GLOBAL FINANCE AND OFFSHORE FINANCIAL CENTERS: A CASE STUDY OF THE ISLE OF MAN

By

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For Artie and the continuance of insatiable curiosity.

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It is widely accepted that the complexity of the global financial system has increased in recent years. This study addressed the way in which this complexity is represented in space, by focusing on one of a large number of small places acting as offshore financial centers (OFC).

A survey of financial practitioners in the Isle of Man was undertaken based upon a theoretical framework meshing elements of the global-local debate, pragmatic regulation, and network analysis. A conceptual framework identifying the major "success" factors for an OFC and the ways in which the local (the Isle of Man) interacts with the global was then developed. Respondents were asked why they thought the island's offshore sector had grown so much over the past decade, what type of niche services were provided, and what type of local-global interaction takes place.

Findings suggest that the major reason for growth was the establishment of a proactive regulatory regime which enabled the island to develop a superior reputation in the world of offshore finance. Public-private interaction through networking activities appeared to be the major driving force behind the establishment of this regime. Survey respondents were concerned about the lack of government efforts at marketing and promoting the offshore financial sector. This concern has been addressed in recent years by the formation of a government Commercial Development office, the establishment of the *IOMplc Roadshow* where both government and private sector officials visit a particular target area for marketing purposes.

Suggestions for future research are threefold: firstly, investigate implications of structural changes in the offshore industry, such as the trend for "one-stop shopping" for financial services; secondly, address other economic development strategies for the Isle of Man itself; thirdly, implement comparative studies with other OFCs to discover if the regulatory regime is the critical factor for growth.

CHAPTER 1
INTRODUCTION

Overview

The evolution of financial services over the past two decades has resulted in a sophisticated and complex global financial system (Bank for International Settlements, 1994; Pavel and McElravey, 1991; Thrift and Leyshon, 1994). This complexity can be linked to the demise of the Bretton Woods system of fixed exchange rates in 1973, the rapid rise of the Euromarkets, the recycling of petrodollars and the rapid advances occurring in information technology and communications (Corbridge, 1994; Goldberg et al., 1988; Lewis and Davis, 1987; Panic, 1995; Strange, 1994; Warf, 1989). Sophisticated means by which money can make more money have exploded over the past few years. New financial instruments such as derivatives have become more complex and less understandable to all but a few City and Wall Street analysts (*The Economist*, 1995; Kelly, 1995).

The functional complexity of the global financial system is mirrored by the system's complex representation in space. Even though it is widely accepted that the world's major international financial centers are London, New York and Tokyo (Hamilton, 1986; Sassen, 1991; Thrift, 1994), capital is flowing around the world in an ever-increasing quest for greater rates-of-return. The fluidity of the financial system of the 1990s has resulted in a large and increasing number of so-called financial centers looking to attract and manage

those rapidly circulating streams of capital. Some of these places are known as offshore financial centers (OFCs)--small island economies often whose only other comparative advantage is tourism. Relatively little attention has been paid to these small places scattered throughout the globe, yet when looked at as a whole, the offshore financial world "captures" a significant amount of circulating investment capital.

This research attempts to begin to redress the paucity of empirical work analyzing OFCs--a field that is still grappling with the theoretical and conceptual underpinnings of the geography of financial services, particularly with respect to offshore financial centers. This research analyzes the growth of OFCs and their position in the global economy by placing empirical evidence from one OFC (the Isle of Man) within the framework of a theoretical mesh of: (1) the global-local debate (Swyngedouw, 1992), (2) pragmatic regulation (Moran, 1991), and (3) the network paradigm (Cooke and Morgan, 1993).

Common threads tying this analysis together will be the analysis and application of the concepts of regulation, networks, trust, and knowledge to the arena of offshore financial centers as those centers strive for continued growth based upon the establishment and maintenance of a *superior reputation.* One of the biggest challenges confronted by OFCs is the establishment and preservation of a reputation among financial services providers and their clients as a safe, confidential, and well-regulated place to do business, particularly as accusations of OFC laundering of drug, mafia, or other "dirty" money abound in the onshore world (Blum, 1984; Courtenay, 1996; Hampton, 1996a).

The recent proliferation of OFCs, combined with the increasing complexity and sophistication of their functional role, has resulted in the perception of the center itself as a

stable and safe place to put money becoming a critical element in the center's survival and success. Some OFCs, such as Cyprus, Antigua, and the Seychelles, have a reputation as dubious and disreputable places where illicit money is stashed, and others, such as Jersey, Cayman Islands, and the Isle of Man, strive to deliberately construct a much more positive reputation (Stewart, 1996; Courtenay, 1996; *The Economist*, 1997a). Fundamental to the reputation of an OFC is the perceived quality of its financial regulatory and supervisory environment. It will be shown that *spatially focused regulation and supervision* in the Isle of Man is developed through a process of continuous public-private interaction using a variety of networking processes.

Research Objectives

Geographically and functionally, small offshore financial centers (OFCs) such as the Cayman Islands or the Isle of Man have experienced both growth and increasing diversity in financial services over the past twenty years. A number of research questions are posed by this significant growth and change. How do the smaller OFCs fit into the global financial system? Are the financial services and instruments employed by OFCs different from those used in London, New York or Tokyo? Why do customers choose to deposit money in OFCs rather than in other larger financial centers?

The purpose of this research is to gain a greater understanding of the role that one OFC--the Isle of Man--plays in the "big picture" of global finance. The Isle of Man is a small semi-autonomous island nation located mid-way between England and Ireland in the Irish Sea (see Figure 1.1). The land area of approximately 220 square miles contained a

population of over 71,700 in 1996 which is the highest population recorded since the Census was first undertaken in 1821. The Isle of Man's (or Manx) economy is now dominated by the finance sector, which has doubled in importance over the past twenty years to comprise 36% of the island's GNP and almost 20% of the workforce (Isle of Man Government, 1996a; Lapper and Stuart, 1996).

The major research questions to be addressed in this study are:

1. How does the island's financial sector link in to the global financial network?
2. What type of niche market (if any) and core competencies does it offer?
3. Why has the Manx financial sector grown so rapidly over the past 20 years?

These questions can be adequately answered only through the collection and analysis of primary data, supplemented by an analysis of secondary data using a mix of quantitative and qualitative techniques (Uzzi, 1996).

Research Outline

Chapter 2 presents evidence of previous research by social scientists and financial economists regarding the global financial system. Following a discussion and subsequent critique of existing theoretical approaches to the study of OFCs, an alternative theoretical framework will be developed. It will be shown that neoclassical, radical, and political economy theoretical approaches offer a macro-level top-down approach to the study of OFCs and fail to consider micro-level growth from within (or bottom-up) approaches to development.

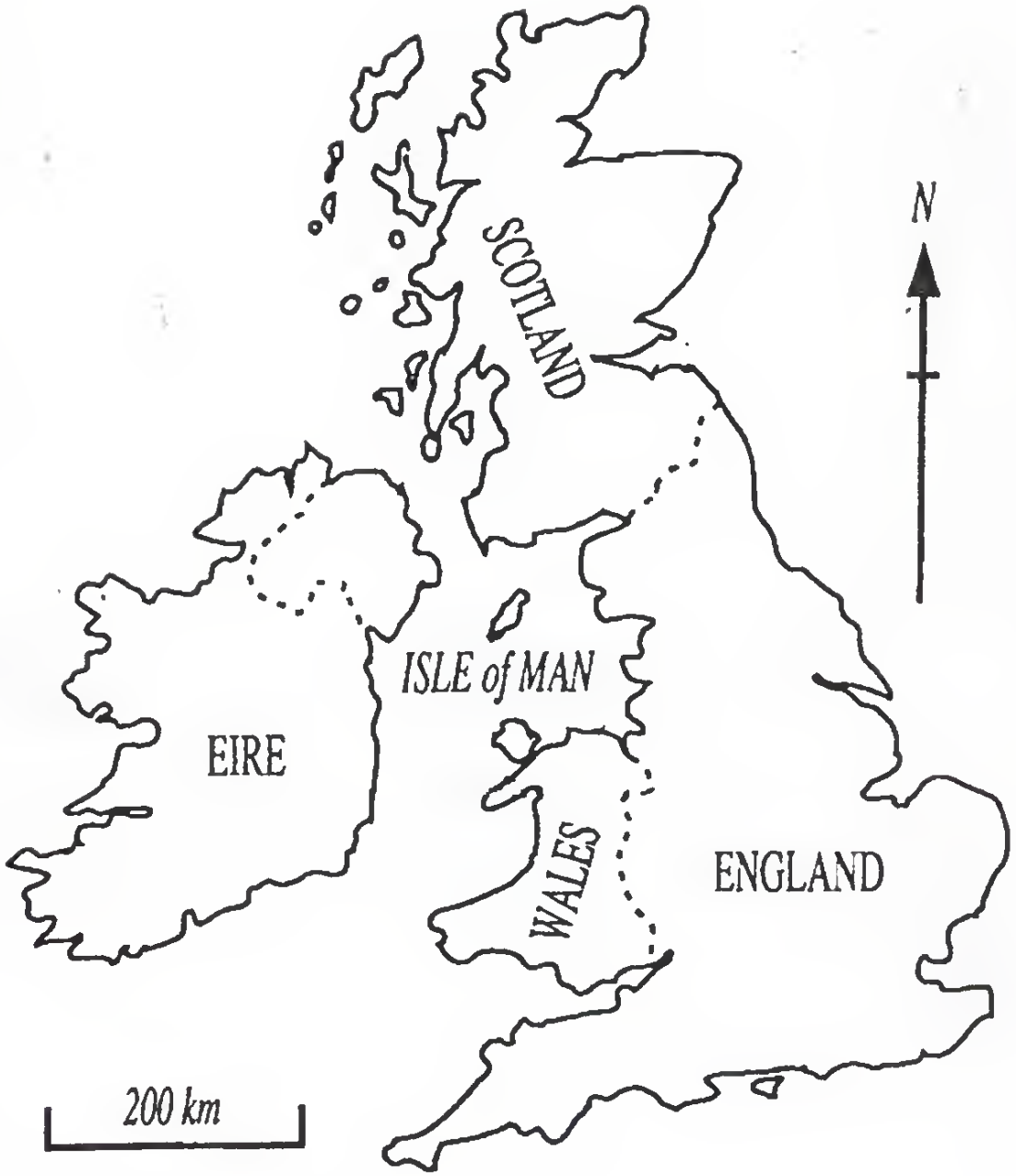

Figure 1.1. The Isle of Man

An alternative theoretical discourse will be developed that, first, addresses the way in which the "local" interacts with the "global" using theoretical foundations from the global-local debate. Second, consideration of the critical role of regulation will be addressed both from a *functional* perspective distinguishing between the "government" versus "marketplace" schools of thought, and from a *spatially focused* perspective as individual OFCs strive to create a regulatory environment to make that OFC more attractive than others. Third, analysis of the way in which such spatially focused regulation is developed and subsequently promulgated will be developed using elements from the network paradigm. One of the major reasons for the use of networks is to facilitate the generation and transmission of knowledge (Malecki, 1997a). Furthermore, the successful functioning of networks is conditioned upon building trust among its members (Yeung, 1994). The establishment of trust and growth of knowledge are tasks more easily done in small places (such as most OFCs) or spatial clusters of companies engaged in providing the same type of service such as the City of London, where everyone knows everyone else of importance (Thrift, 1994).

Chapter 3 develops a conceptual framework to further the understanding of the position of OFCs in the global financial system by addressing the ways in which these (usually) small places link into the global economy. It is shown that local-global linkages can be conceptualized along three dimensions: location, function, and regulation. In addition, Chapter 3 presents a methodological framework used to gather empirical evidence from a case study of the Isle of Man and sets the stage for analysis of survey results by documenting the initial development and growth of the island as an OFC in the 1960s and 1970s.

The empirical findings from the Isle of Man case are analyzed in Chapters 4, 5, and 6 and attempt to mesh evidence with the theoretical frameworks developed in Chapters 2 and 3. Chapter 4 analyzes evidence supporting the rapid growth of the Manx offshore sector during the 1980s and into the 1990s; Chapter 5 addresses the perceived reasons for this growth; and Chapter 6 documents current marketing strategies established by the island to ensure future growth. Specific reference is made to the deliberate creation of an appropriate regulatory environment in the Isle of Man. Results from a study of 71 financial service providers and regulators in the Isle of Man show that the island's current regulatory regime is the result of deliberate public-private interaction aimed at improving the image and reputation of the island as an OFC. Public-private collaboration has facilitated the development of a proactive regulatory regime designed to promote stable, reputable growth in the financial services sector. Furthermore, public-private interaction is used to develop and implement marketing strategies for *Isle of Man plc* with the aim of promoting the island and increasing awareness of the island and the niche products and services offered here and nowhere else.

Conclusions and directions for further research are presented in Chapter 7. Avenues for future research are considered along three directions: first, is a consideration of structural changes within the financial services industry and how these changes may be used for further gain by the offshore world. Second, suggestions of economic strategies for further growth and development of the Isle of Man's offshore financial sector will be offered. Third, directions for future research of the offshore financial sector in general will be offered with the aim of applying the research method presented in this study to other OFCs.

CHAPTER 2
GLOBAL FINANCE AND OFFSHORE FINANCIAL CENTERS

The Global Financial System

> If there is any arena of economic activity that has become global in recent decades, it is finance. Modern means of communication...help transfer vast sums of money across national boundaries every day. Money moves faster and in response to smaller price differentials than do goods or people (Herring and Litan, 1995, p. 1).

> The 'new international monetary system' is a system in which the evident volatility of interest and exchange rates, not to mention capital movements, is countermanded by new financial institutions and new instruments designed to share risks and to provide insurance for the market's major players (Corbridge and Thrift, 1994, p. 11).

The ease with which capital can flow around the globe has increased dramatically over the past two decades. This increasing fluidity of capital has been ascribed to several factors, including the breakdown of the Bretton Woods system of monetary order, the increasing use and sophistication of telecommunications technology, and the rise of a system of spatially differential financial regulatory practices throughout the world (Corbridge 1994; Warf, 1995; Edwards and Patrick, 1992).

The new mode of operation of the global financial market is reflected by the use of increasingly sophisticated financial instruments invented over the past two decades to "attain exactly the right articulation of time, space, and risk" (Thrift and Leyshon, 1994, p. 303). The rapid rise and importance of derivatives--defined as "complex financial instruments whose values derive from other assets and indices of these asset values" (ibid)--such as

futures contracts, swaps, options, "swaptions" and the like, has resulted in a degree of global disorder as the world's financial regulatory and supervisory regimes struggle to come to grips with the risk and complexity of these mechanisms (*The Economist*, 1995).

The financial services sector has been described as "totally fundamental to the operation of every aspect of the economic system" (Dicken, 1992, p. 358). However, until recently, most research on the finance sector occurred within the domain of financial economics and, not surprisingly, was driven by the neoclassical theoretical perspective (Aliber, 1984; Bird, 1990; Mullineux, 1987; Silber, 1975). The financial system was seen as the outcome of an ordered, logical process driven by the aim of accumulating capital through the behavior of utility-maximizing individuals and firms. Traditional neoclassical economic interpretations of the global financial system form the core of research in the business and finance world (Aliber, 1980; Crane and Hayes, 1983; Johns, 1983; Johns and Le Marchant, 1993; Kapstein, 1994; Walter, 1988).

The rapid growth and importance of the finance sector was largely ignored by economic geographers until recently when the *globalization* of financial services stimulated recognition of the need for a new understanding of this increasingly complex, flexible, and uncertain system (Leyshon, 1995; Leyshon and Tickell, 1994; Thrift and Leyshon, 1994). Only over the past decade has serious research taken place on this aspect of the global economy by economic geographers; theoretical debate is still in the formative stage and empirical evidence is relatively sparse.

Perhaps the greatest contribution by geographers is (and will continue to be) the development of an alternative approach to the analysis of global finance and financial

services. Geographers search to make sense of a world that is increasingly complex, flexible, and uncertain-- possibly more so in the field of finance than any other part of the global economy. The globalization of financial services heralds the need for a new understanding of this increasingly complex system (Clark and O'Connor, 1997; Corbridge, 1994; Corbridge and Thrift, 1994; Leyshon and Tickell, 1994; Thrift, 1994; Thrift and Leyshon, 1994).

Leyshon (1995) believes that "the growth of geographical treatments of money and finance may be seen to have developed in lockstep with the growing economic, social and cultural prominence of the financial system during the 1980s and 1990s" (p. 531). Leyshon highlights research on the geographies of money and finance by examining political economy approaches to the subject, focusing on issues of the geopolitical economy of finance, the geoeconomics of finance, and the geographies of financial exclusion. Not surprisingly, so far the role of geographers has been greatest in the third of these issues, which is inherently the most spatial (Leyshon and Thrift, 1994; Pollard, 1996).

Consensus is widespread regarding the spatial and functional complexity of the global financial system. The spatial organization of financial services appears to be a synthesis of order and disorder depending on the scale of analysis. Even though it has been argued that the powerful impact of information technology implies the "end of geography" (O'Brien, 1992), the largest and most important financial centers in the world are widely recognized to be the "world cities" of New York, Tokyo, and London (Friedmann, 1986; Hamilton, 1986; Lewis and Davis, 1987; Martin, 1994; Sassen, 1991, 1994; Thrift, 1994).

A lack of consensus exists, however, on a method to describe adequately the relative importance of the world's other financial centers. Should the system be defined as the three

primary world cities with everything else subordinate (Hamilton, 1986) or as a distinct hierarchy based upon volume of capital flows (Dicken, 1992; Friedmann, 1986)? In a hierarchical system based upon volume, should the spatial scale be nodal--Chicago, Paris, Los Angeles, Frankfurt, Sydney, Singapore, Hong Kong--or regional--Switzerland, Luxembourg, Germany, Canada (Martin, 1994; Reed, 1981)?

This research will adopt a "nodal" approach by focusing upon the increasing number of much smaller financial centers--in particular small island OFCs. At this lowest level in the hierarchy of financial places, the system appears quite murky—even confused—with a large and ever increasing set of smaller financial centers dispersed across the globe (see table 2.1). Most of these smaller places—for example, the Isle of Man, Cayman Islands, Jersey, and Bermuda—function as "offshore" centers where the majority of capital invested belongs to non-resident institutions or individuals (Burt 1995; Johns 1983).

Regarding the position of OFCs in the global financial system, there is debate as to whether they should (1) comprise the lowest level in the hierarchy (Arndt, 1988), (2) be considered independently of the "big spatial picture" (Holstrom, 1988; Moore, 1992; Walter, 1985) or (3) be linked into the global financial system (Roberts, 1994, 1995). This study will address, among other issues, ways in which OFCs interact with the global economy.

OFCs have to strive hard to become accepted into the global system of finance by creating superior reputations as stable, secure, yet confidential places to invest money. The key to establishing a quality reputation is the formation of an appropriately balanced regulatory and supervisory framework for financial services. Those places that choose not to establish rigorous regulatory and supervisory frameworks geared towards attaining global

standards, such as those established by the Basle Committee for Banking Supervision, are often the ones accused of money laundering, crime, and corruption (Quirk, 1997).

Table 2.1. Offshore financial centers

EUROPEAN REALM	CARIBBEAN REALM	ASIAN-PACIFIC REALM	OTHER
Andorra	Anguilla	Cook Islands	Bahrain
Campione	Antigua	Hong Kong	Kuwait
Cyprus	The Bahamas	Labuan	Lebanon
Dublin	Barbados	Marshall	Liberia
Gibraltar	Belize	Islands	Mauritius
Guernsey	Bermuda	Nauru	United Arab
Isle of Man	British Virgin	Philippines	Emirates
Jersey	Islands (BVI)	Singapore	
Liechtenstein	Cayman Island	Taipai	
Luxembourg	Costa Rica	Tonga	
Madeira	Dominica	Vanuatu	
Malta	Grenada	Western Samoa	
Monaco	Montserrat		
Netherlands	Netherland Antilles		
San Marino	Nevis & St. Kitts		
Switzerland	Panama		
	St. Lucia		
	St. Vincent		
	Turks & Caicos		
	Uruguay		

Source: adapted from Hampton 1996c; Davis, 1994; Roberts, 1994

Until recently, little attention has been paid to the small--literally "offshore"--financial centers (OFCs) that are found scattered throughout the world and little work has been done to provide any empirical evidence from a "bottom-up", i.e., a place-focused perspective. Many such places exist and even though when each, looked at individually, may be insignificant in terms of the amount of capital invested there, when considered as a whole,

play an important role in understanding the workings of the modem financial system (Lewis and Davis 1987). According to Diamond (1994), offshore financial bases service an estimated $5 trillion of investment funds each year.

Offshore Finance and Offshore Financial Centers: A Critique

> In the past six years offshore financial centers have become increasingly important to the intemational financial system. They have also come to be regarded with greater respect . . . Today, offshore financial bases have an estimated US$5 trillion of investment funds and are a powerful necessity in the daily operations of multinational corporations, small and medium-size companies, banking institutions and executives in the legal, accounting and investment counseling professions (Diamond, 1994, p. 22).

The new phase of capitalist development which is emerging in the post-Bretton Woods era is characterized by increased capital mobility and the rise in importance of offshore markets (Amin, 1994; Gill and Law, 1988; Guttmann, 1994). "Offshore" markets had their origin with the decline of U.S. hegemony[1] that characterized the Bretton Woods system of fixed exchange rates and the subsequent desire of American institutions and individuals to circumvent their restrictive banking system and search for increasing rates-of-retum elsewhere. This stimulated the growth of the "Eurodollar" market centered on London where Americans deposited U.S. dollars outside the U.S. (Greenbaum and Thakor, 1995; Lewis and Davis, 1987; Martin, 1994). Today, the Euromarket concept has broadened to include many currencies in many markets—the key element being the placement of capital

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[1]Many argue that U.S. hegemony exists in a reconfigured format as the post-Cold War world has placed the U.S. at the forefront of the global economy with unchallenged economic and political power (see Agnew and Corbridge, 1995; Hancher and Moran, 1989).

outside the individual's or institution's country of residence. Moreover, "offshore markets are markets for currencies, loans, bonds and a host of other financial instruments which exist *beyond the reach of regulation* by the original national economies" (Roberts, 1994, p. 93; emphasis added).

But how is this fundamentally "aspatial" system, where credit-money (Guttmann, 1994) is mysteriously moved from one financial market to another, revealed geographically? While the ownership of money is usually beyond doubt, the *control* of flows of money passes from the owner to a financial "manager." In the control of the "manager," a flow of credit-money may pass from financial center to financial center (onshore and offshore places) in its quest for greater rates-of-return. How many places and which places are involved, and exactly who makes the decisions as to how the money is invested? The intricacies of this spatial process have, to this point, defied understanding, as evidenced by the actions of so-called "rogue traders" and, more recently, fund managers operating throughout the world (*The Economist*, 1996a)[2].

The role played by OFCs and their linkages into the global economy were explored by Roberts (1994), who argues that the formation of OFCs is tied to the growth and development of the Euromarkets themselves. As the total amount of capital invested "offshore" has increased over the past two decades, so has the total number of offshore *places* increased. However, widespread consensus regarding the absolute number of such places is hindered by the lack of a single accepted definition of an OFC. The 1994 edition

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[2]Clark (1997) provides a thought-provoking analysis on the "demonization" of such persons and the "problems of dealing with so-called rogue behavior in the context of [financial] regulation and regulatory regimes" (p. 221).

of *The International Offshore and Financial Centers Handbook* covers 26 jurisdictions, but other classifications place the number of OFCs significantly higher than this. Table 1.1 (see back) shows 52, Diamond (1994) refers to 61 tax havens, Hampton (1996c) lists 43 main tax havens, and Roberts (1994) also classifies 43[3].

Roberts (1994) recognizes that OFCs may be classified in terms of their volume of services and differentiates between major OFCs (for example, Hong Kong, Singapore, Panama) and minor OFCs (for example, Malta, Netherlands Antilles, Vanuatu). Roberts goes further to introduce the critical element of *spatiality* into her analysis. She illustrates that the global distribution of OFCs can be thought of as a series of "regional clusters" using time zones as the most obvious reason for such groupings. Each major regional cluster is aligned with its nearest world city, for example, the Caribbean OFCs with New York and the European OFCs with London. Table 1.1 is organized in terms of geographic realms using similar rationale to Roberts' work. Figure 2.1 illustrates the global distribution of small island OFCs based on Hampton's (1996b) work.

A current definition of an OFC is "a center that hosts financial activities that are separated from major regulating units (states) by geography and/or by legislation. This may be a physical separation, as in an island territory, or within a city such as London or the New York International Banking Facilities (IBFs)" (Hampton, 1994, p. 237).

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[3]Roberts' classification is, however, different to Hampton's as Roberts includes mainland and island OFCs, whereas Hampton only considers small island OFCs.

1 Isle of Man
2 Jersey
3 Guernsey
4 Malta
5 Cyprus
6 Bahrain
7 Gibraltar
8 Mauritius
9 Labuan
10 Marshall Islands
11 Nauru
12 Vanuatu
13 Western Samoa
14 Cook Islands
15 Bermuda
16 Bahamas
17 Cayman Islands
18 Anguilla
19 Antigua
20 Barbados
21 British Virgin Islands
22 Dominica
23 Grenada
24 Montserrat
25 Netherlands Antilles
26 Nevis & St. Kitts
27 St. Lucia
28 St. Vincent
29 Turks & Caicos

Figure 2.1 Global distribution of small island OFCs
Source: adapted from Hampton (1996c).

One classification of OFCs is provided by Hampton (1996c), following McCarthy (1979), who proposes "tiers" of OFCs comprising *functional* (where a variety of financial activities actually take place), *notional* ("brass-plate" offices that make book entries of financial activities), and *compound* (a mixture of both).

Fisher (1994) identifies eight categories of offshore centers or tax havens driven by different levels of taxation:

1. nil tax regimes;

2. traditional tax havens that do not impose a tax on profits;

3. low tax regimes;

4. low tax countries that impose a relatively low rate of tax on profits but have special exempt regimes for international and offshore business carried out in the islands;

5. no tax on foreign source income (a strict territorial basis of taxation);

6. privileged tax regime territories, which have high rates of local tax but have special tax regimes and incentives for certain operations such as mutual funds, holding or finance companies;

7. retirement havens for high net worth individuals (HNWIs);

8. tax planning havens that can sometimes be exploited by residents and non-residents in a tax efficient manner.

The key to the existence of OFCs, notwithstanding the definitional problems, is the notion of capital placed and managed *outside and beyond* an institutions' or individuals' onshore regulatory regime. This case-study example (the Isle of Man) is classified by Hampton

(1996c) as a "functional" OFC, by Roberts (1994) as a "major" OFC, and by Fisher (1994) as a "low tax" country.

Analysis of the creation and growth of "offshore" financial places is limited to a handful of researchers, each using quite divergent theoretical and conceptual frameworks. Johns (1983), Johns and Le Marchant (1993), Doggart (1979), McCarthy (1979) and Walter (1985) provide traditional neoclassical interpretations of the existence and growth of OFCs. Hampton (1996a, 1996b) uses a political economy approach, Roberts (1994, 1995) uses a more radical framework, drawing upon seminal works by Harvey (1982, 1989). Most work (including the findings from this study) is of a case-study nature and, as yet, a firm theoretical basis underlying the rationale for the existence of OFCs has yet to be developed.

Neoclassical analysis of the growth of OFCs in the global economy draws theoretical foundations from Kindelberger's (1974) work on the creation of international financial centers. Factors of comparative advantage such as minimization of transactions costs for transnational corporations in the arena of international business were seen as the driving force behind the establishment of such places. The neoclassical approach as applied to *offshore* financial centers stressed similar theoretical logic, often resulting in predominantly descriptive listings of "advantages" of one OFC over all others (Johns, 1983; Johns and Le Marchant, 1993; Doggart, 1979; McCarthy, 1979).

Hampton (1996c) argues that neoclassical location theory, particularly with respect to the further development of an established OFC through agglomeration economies, makes a valid contribution to understanding the *growth* of OFCs in the global economy, but does not go far enough. Criticism of the neoclassical approach focuses on the inability of these

discourses to explain why OFCs developed in the first place (Gorostiaga, 1984; Hampton, 1996c). Furthermore, the dismissive nature of factors of location that cannot be easily measured or quantified, such as the development of differential regulatory and taxation regimes (see Reed, 1981; Goldberg et al., 1988), is seen as a major flaw.

Gorostiaga (1984, introduction) argues that a more radical approach to the study of financial centers is needed and that "IFCs [international financial centers] will be analyzed as the product of changes in the very nature of capital itself and in the organization of capitalism at the center of the system" and not as endogenous phenomena. Roberts (1995, p. 237) attempts "to further a Marxian understanding of how capital increases its flexibility and averts crisis (not unproblematically) through the financial system." This new system, according to Roberts, produces new spatial forms or, in her words, new regulatory spaces, asserting that "in the financial markets, spatial advantage may be defined primarily through regulation" (p. 252).

Hampton (1996c, p. 136) promotes a radical political economy approach by analyzing the "significance of the primary attractions of taxation, regulation (or deregulation) and the *underlying political relationship of the island or microstate to its nearest 'Big Brother' country"* (emphasis added). The importance of Hampton's contribution to the theory of OFCs in the global economy is twofold: first, he is concerned with the evolution of an OFC and argues that

> In the early stages of OFC development the lack of many other financial services could act as a deterrent to new arrivals. Other factors aside from location, such as regulation, taxation or secrecy, may therefore initially attract a financial services firm to a new OFC. Location thus appears to be of lesser importance in the first stage of emerging OFCs than the major factors of taxation, bank secrecy, regulation and the

> political situation and there would seem to be some sort of moving sequence with different factors influencing spatial location at different times (1996c, p.134).

Second, Hampton employs a neo-Marxist "fractions of capital" approach to argue (using Jersey as his case-study) that the special relationship existing between mainland states and their offshore territories is central to the development of offshore finance.

The weakness of so-called radical analysis is the inherent top-down macro-level focus of the neo-Marxist structural approach and concomitant lack of consideration of "bottom-up" approaches. The notion that change can be affected from within, or at the micro-level, through the existence of proactive local actors and institutions is ignored. It is argued here that the creation and growth of OFCs is a function of global forces *and* local actions and this research will subsequently derive a theoretical framework based upon elements of the *global-local debate*, *regulation*, and *network analysis*.

Functionally, many of the older established OFCs such as the Cayman Islands or Jersey have experienced both growth and diversity in financial services over the past twenty years. The concept of a "generic" OFC or tax haven no longer exists. Furthermore, "there is no single offshore center which will be all things to all people . . . users of offshore centers . . . are becoming more sophisticated at selecting the appropriate center for their particular operations" (Fisher, 1994, p.21). One of the recurring themes that will be shown in this study is the attempt by public *and* private organizations in the Isle of Man to develop new and innovative financial products for particular niche markets.

The Rise of OFCs: A New Theoretical Interpretation

Existing theory of OFCs either adheres to the traditional neo-classical interpretation of factors of comparative advantage (Johns, 1983; Johns and Le Marchant, 1993) or to variants of the radical critique of capitalism (Gorostiaga, 1984; Hampton, 1996a,b,c; Roberts, 1994, 1995). It has already been shown that neither approach fully accounts for the rise of OFCs and their successful linkages into the global economy. This research project will attempt to provide an alternative theoretical framework by meshing elements of three different theoretical discourses: the global-local debate, regulation, and network analysis.

The Global-Local Debate

Insight into the complex spatial tensions of the global economy in the 1990s has been provided in part by the global-local debate (Peck and Tickell 1994): one of the theoretical threads running through current discourses is the dialectic of "locality and globality" (Lipietz 1993, p. 8). Swyngedouw (1992, p. 40) describes the local-global phenomenon as "a double movement of globalisation on the one hand and devolution, decentralisation or localisation on the other". This phenomenon has been given the name "glocalisation". It is seen by Peck and Tickell (1994) as a process of *disorder* as places function to compete against each other in the global economy, driven by the underlying dominant politico-economic order of neoliberalism.

Amin and Thrift (1993, p. 405) contribute to the local-global debate through "consideration of the way in which globalisation and local development are locked together

at an institutional level". For Amin and Thrift, globalisation represents "a redefinition of places as juxtapositions of intersecting, overlapping and unconnected global flows and historical fixities" (1993, p. 411). But what makes one specific place (the local) *better* at fitting in, and successfully participating in, the global than any other place? Amin and Thrift argue that successful local development within the global economy is driven by "institutional thickness"--the amount, variety, vibrancy, enthusiasm, and level of interaction of institutions within a specific place. The melting pot of institutions is place-unique and serves to differentiate between those places that can and those that cannot successfully participate in the global economy.

The application of these macro-economic discourses to global finance and the growing importance of OFCs in the global economy is limited. Johns and Le Marchant (1993), in their study of the development of the British Isles' offshore financial centers (Jersey, Guernsey, Isle of Man), conclude that

> Island govemments must be alert to the possibility of institutional divestment and to the fact that their mesoeconomic actors are not obliged to have local national loyalties: their allegiance is to their *global company advantage* and not to a specific territorial advantage (p. 276, emphasis added).

Roberts (1995, p. 254), in her work on the Cayman Islands, is more cognizant of the global-local phenomenon, stating that

> OFCs are spaces that exemplify the contradictory movements toward global integration (as the flows of capital around the globe move faster and faster, for example) and local variation and fragmentation (as places act entrepreneurially to exploit niches in world markets and as capital hones its ability to arbitrage difference).

Lipietz (1993) contends that "there can only be a certain type of 'regions which win' within the framework of a certain type of nation state . . . and these states will only 'win' in international economic competition if *they know how to create* this type of regions which win" (p. 16, emphasis added). Can this theoretical logic be applied to very small nation states offering a particular type of economic service, i.e., the OFC?

For OFCs the creation of "regions which win" can only occur through the creation of a superior reputation driven by establishment of an appropriate financial regulatory and supervisory regime. In the world of offshore finance, a superior reputation develops when *spatially focused regulation* is created through the cooperation of the public and private sectors of the economy. Such regulation is designed to create a specific regulatory environment that is somehow *different* from other places. This regulation aims to "reconcile contradictory needs for safety and innovation" (Burgess, 1997, p. 73).

Moran (1991) explores the notion of a *system of regulation* of financial services by asserting that

> competitive conditions in financial services are uniquely sensitive to regulatory arrangements because the 'goods' traded are themselves mostly regulatory creations - contracts, legally binding or otherwise, embodying a structure of financial claims and obligations . . . systems of regulation are themselves *powerful sources of comparative advantage* (pp. 6-7, emphasis added).

The importance of the system of regulation and the significance of the creation of a balanced regulatory and supervisory regime for an OFC will be analyzed in the next section.

Regulation

> Regulation is virtually a defining feature of any system of social organization . . . it involves the design of general rules, the creation of institutions responsible for their implementation, the clarification of the exact meaning of a general rule in particular circumstances, and the enforcement of the rule in those circumstances (Hancher and Moran, 1989, p. 271).

> The financial world has become one in which services that cannot be provided onshore are provided offshore, those that cannot be provided on the balance sheet are provided off the balance sheet, and those that cannot be provided with existing instruments are provided with new ones . . . supervisors have shown that they are aware of the need to keep up, but can they? (Mullineux, 1987, p. 60)

Regulatory issues are of critical importance in the changing world of international finance. As the global financial system becomes more complex and capital flows around the world at an ever increasing pace, both regulation and supervision of the financial sector have become issues of concem among social scientists as well as those in the finance and business world (Bird, 1990; Coleman and Porter, 1994; Gentle and Marshall, 1992; Goldberg, 1994; Hayes, 1993; Kim, 1993).

Many social scientists have embraced "Regulation Theory" as a way of further understanding the capitalist crisis of post-Fordist flexible accumulation (Aglietta, 1979; Lipietz, 1987; Peck, 1994; Tickell and Peck, 1992; Smith, 1995). Proponents of regulation theory argue that the complexities within the global economy can best be analyzed by addressing the specific *regime of accumulation* (Fordist and Taylorist assembly-line practices rather than post-Fordist flexibility) and *mode of social regulation* (socio-economic conventions and practices) present within society at any given time. Thrift (1994) states that

the form of the mode of social regulation can vary over time and space and, more importantly, that regulation theory can be used to identify and analyze "the connection between the success of economies and their pattems of social regulation" (p. 371).

Debate exists, however, regarding the rationale for, and uses of, regulation theory. For example, Murdoch (1995) argues that regulation theory is a "macro account and concentrates on how micro phenomena are 'pulled' into place within specific regimes" (p. 734). On the other hand, Smith (1995) asserts that "there are many sites of regulation and that these various 'regulatory sites' are influenced both by state and non-state institutions and interactions between agents which constitute an economic system" (p. 761).

Most regulation theorists acknowledge that relatively little research has been undertaken on the mode of social regulation under the new regime of flexible accumulation (Peck and Tickell, 1992; Peck, 1994; Smith, 1995; Yeung, 1994). Although regulation theory is perceived by many as being robust and applicable to many of the complexities of the modem economy, it is the lack of theoretical consensus and validity with respect to the mode of social regulation--surely the most important piece of regulation for finance, and particularly for OFCs--and the inherently macro-level focus, that makes it unsuitable for use in this study. The study of offshore financial regulation in particular has to recognize the pragmatic nature of regulation--regulation that takes into consideration the human precepts of trust, confidence, familiarity, and security at the *local level* as well as the global.

Differential spatial regulation implies that growth is likely in those financial centers that have deliberately chosen to construct attracting regulation, especially small OFCs that have a politically dependent relationship with a larger state. Roberts (1994) considers such

OFCs as "groups of marginal places . . . which exist as adjuncts to one of the three financial blocs centered for the moment on London, Tokyo and New York" (p. 101). The British Isles OFCs--"Crown Dependencies"--of the United Kingdom fit neatly into this category (Hampton, 1994, 1996c; Johns, 1983; Johns and Le Marchant, 1993).

The creation of an appropriate financial regulatory regime hinges upon functional regulation of the *services* provided by firms within the sector. For example, banking institutions in the world's largest economies are regulated via standards imposed by the Basle Concordat. Similar global functional regulation is provided for international securities transactions by the International Organization of Security Commissions (IOSCO). An additional supranational organization, the Enlarged Contact Group (ECG), regulates collective investment schemes (mutual funds or unit trusts) and their operators. Furthermore, insurance providers are regulated by the International Association of Insurance Supervisors (IAIS) (Bhala, 1994; Isle of Man Financial Supervision Commission, 1995, 1996; Shirreff, 1996).

For international banking, the most important regulatory development of the 1990s, one which recognized the increasingly global characteristics of the modern financial system, was the 1988 Basle Agreement by the Group of Ten leading industrial nations to impose uniform capital standards for banks (Coleman and Porter, 1994; Guttmann, 1994). By the end of 1992, banks operating in those countries were supposed to maintain capital equivalent to 8 percent of assets, weighted by risk. This international convergence of capital adequacy measurement and standards "may be regarded, therefore, as a significant milestone in the establishment of a common supervisory response to the existence of a single, highly

competitive, international banking market" (Cooke, 1990, p. 311). Herring and Litan (1995) argue that:

> the Basle standards have helped make disclosure of the financial conditions of banks around the world more uniform, a result that has enhanced the effectiveness of market discipline (by facilitating comparison of banks by depositors, creditors, and shareholders).

However, it is also recognized that the Basle Accord in and of itself has limitations. Most importantly, the Basle countries form an exclusive club: the agreement does not apply to many industrialized countries and no less-developed countries belong. Breeden and Isaac (1992) go so far as to assert that risk-based capital rules were a mistake. In addition to distorting credit flows, those standards may *create* a potentially serious safety and soundness problem by altering a bank's portfolio of risk-management strategies or exposures.

Debate exists regarding the underlying rationale behind financial regulation. Kopcke (1995, p. 37) asserts

> Current discussions, like those in the past, engage views of financial markets that are difficult to reconcile. Some, who believe that these markets potentially are relatively efficient, advocate minimal interference. Regulations that require more than the necessary disclosure of investments and risks might introduce burdens that exceed their benefits. Others, who believe that the predominance of intermediaries reflects the limits of savers' information, advocate regulation to ensure the safety and soundness of intermediaries. At the very least, regulations may diminish the force of "credit cycles" and the threat of widespread insolvency among intermediaries.

Stiglitz (1993) believes that there is a necessary role for the state in financial markets because potential market failures are likely to be pervasive. He argues that "there exists forms of government intervention that will not only make these markets function better but will also improve the performance of the economy" (p. 20).

Government intervention is most evident with respect to banking regulation as virtually all aspects of the operation of a bank are subject to government oversight and regulatory restriction (James, 1995). This is deemed necessary because of the widely held view that banks play a special role in the national, and increasingly international, economy as providers of transaction services and as sources of liquidity (Greenbaum and Thakor, 1995; Lewis and Davis, 1987).

Consensus exists regarding the most critical element of banking regulation: bank safety and soundness (Borio and Filosa, 1994; Eisenbeis, 1990; Lemieux, 1993; Mullineux, 1987). The "safety and soundness" argument has been particularly relevant for banks, where a lender of the last resort (usually a country's central bank) refinances banks' illiquid asset portfolios when other funding sources are unavailable or prohibitively expensive. In addition, many countries have deposit insurance, and also guarantee the integrity of the payments and clearing system (Greenbaum and Thakor, 1995). This consensus is based, however, on a relatively restricted foundation as "almost all the theoretical literature in the field of [banking] regulation . . . derives from an examination of the American experience" (Bourke, 1990, p. 144). The American banking system is unique in its makeup and is currently undergoing significant regulatory reform, in particular with respect to attempts to repeal of the Glass-Steagall Act separating commercial and investment banking in order to "level the international playing field" for American banks (Asher, 1995; Kwan, 1995).

An alternative school of thought regarding financial regulation is that minimal institutional involvement should occur and a reliance on market efficiencies should be used to regulate the system. Flannery (1994, p. 313) asserts that "private (market) regulatory

services provide credible altematives to traditional government regulation". He believes that whereas govemment controls tend to be restrictive and inflexible, market controls provide a *schedule of alternative restraints* from which the least costly ones may be chosen. Flannery's approach is to compare the financial sector to the corporate sector and to argue that the methods by which the corporate world have chosen to regulate themselves (via contracts, covenants, monitoring, evaluating, controlling and pricing risk) could be adapted and used in the financial sector. Although Flannery argues against complete governmental withdrawal of govemment regulation, he argues strongly for "the notion that market investors can perceive bank risks accurately, and hence could provide adequate supervision if the government curtailed its existing insurance coverage" (ibid, p. 323). Borio and Filosa (1994, p. 31) raise the issue of the

> search for an appropriate *balance* between official involvement and market discipline. The broadening of the range of banks' activities within the financial sector and of their ownership linkages with non-financial companies carries the risk of extending the "safety net" generally put in place to prevent systematic crises. Market participants' incentives to prudent behavior may thereby be blunted (emphasis added).

What is needed, therefore, is prudential regulation and adequate supervision by regulatory agencies. However, the dynamic and complex nature of the modem financial system renders it difficult, if not impossible, for regulators to keep up with changes, particularly with respect to financial products and financial engineering. Current research by financial economists indicates a concern for the ability of financial regulation to keep up with the changing features of the global financial system (Berger et al., 1995; Bourke, 1990; Eisenbeis, 1990; Guttmann, 1994; Herring and Litan, 1995; Marshall et al., 1992).

Challenges facing the regulators and supervisors of such a diversified international system include: developing the ability and the resources to regulate large geographically and functionally diversified corporate networks; existing lack of understanding of complex trading risks; and lack of ability to assess management and control elements of financial institutions (*The Economist*, 1996b).

One of the major dilemmas faced by financial regulatory bodies is how, and by whom, the vast array of cross-border flows that comprise the bulk of the modern financial system should be regulated (Edwards and Patrick, 1992). Concern with regulation and supervision of financial conglomerates--both within and *across* national borders--also has been raised by Borio and Filosa (1994). They are especially concerned about the existing highly compartmentalized prudential supervisory frameworks, and the increased possibilities of "contagion" risk occurring within conglomerates. To counter this, "supervisors should be in a position to access information about the various group units, including *unregulated* ones" (p. 22, emphasis added). Possible solutions proposed by the authors include: (a) consolidated supervision, and (b) harmonization of capital standards across function within the conglomerate.

Proponents for change in the way financial services are regulated stress the need for greater cooperation between the various functional regulators (*The Economist,* 1996c; Shirreff, 1996). One of the major problems to be addressed is the diversity of financial functions now provided by a single institution. For example a banking conglomerate may offer insurance and mutual fund services in addition to traditional banking services such as deposit taking and loan making (Eisenbeis, 1990; Hayes, 1993; Metais, 1990). Shirreff

(1996, p. 48) advocates "more coordination between regulators, better information gathering and sharing, and swifter procedures for dealing with anything that threatens to jolt the financial system".

Regulation of an Offshore Financial Center

Tensions in the regulatory process evident in the above macro-economic discourses can also be analyzed first in terms the development of spatially focused OFC regulation and supervision and second in terms of "onshore-offshore" finance (Hancher and Moran, 1989). The complexity of the modern financial system is characterized in part by the rise in importance of "offshore" markets with no national allegiance (Amin, 1994; Gill and Law, 1988; Guttmann, 1994). As no national regulatory body can adequately supervise and monitor cross-border capital flows, the responsibility of regulation must therefore *de facto* fall to some kind of supranational institution.

Even though some have argued that the workings of the modern financial system implies the end of geography (O'Brien, 1992), others argue that place still matters (Leyshon, 1995; Swyngedouw, 1992; Thrift and Leyshon, 1994). The importance of "place," however, can be seen even within the evolution of supposedly aspatial offshore markets. For example, London was the first and consequently the most important center of the Euro- (or offshore) dollar market in the 1960s and 1970s (Mullineux, 1987; Sassen, 1991; Thrift, 1994b). In the 1990s, though, other places became important centers of offshore markets, such as the Bahamas and Cayman Islands for Euro-dollar markets and Singapore for the Asian-dollar market, in part because of *regulatory issues* (Martin, 1994; Pavel and McElravey, 1991;

Stiglitz, 1993; Tan, 1989). This change in location signaled a shift from placeless offshore markets to a proliferation of offshore financial centers (OFCs) which served as nodes in the offshore marketplace as well as the basis of local economic development strategies of (usually) small spatial entities.

OFCs are perceived by many to have less stringent regulation than that found in the "onshore" world (Doggart, 1979; Hamilton, 1986; Hampton 1994; Johns and Le Marchant, 1993; Kinsman, 1978; McCarthy, 1979; Roberts, 1995, 1994; Walter, 1985). In many instances, the main function of OFCs is to provide services for individuals and institutions wishing to escape the regulatory practices of their "onshore" places of residence. Roberts (1994) considers such OFCs as marginal places existing as adjuncts to London, Tokyo and New York". Seen in this light, the reputation of the center is critical and current efforts are underway by many OFCs to improve their "image" by imposing more rigorous regulatory standards (Courtenay, 1996, Stewart, 1996).

Small island offshore financial centers--places at the margins of the global economy --have to try much harder than major financial centers, such as London and New York, to establish and maintain their reputation as safe and secure places to do business in the world of global finance. It is widely recognized that a major factor at stake in an OFC is the reputation of the center itself, leading to *spatially focused regulatory aims.* In Europe for example, many of the older small island OFCs, such as Jersey and the Isle of Man, have established their own regulatory bodies (the Financial Services Commission, and the Financial Supervision Commission respectively) that seek to enhance the reputation of the *place* through actively regulating and *supervising* those providing financial services

(Hampton, 1996b; Solly, 1994). Moreover, the Isle of Man's Financial Supervision Commission goes so far as to acknowledge that "reputational risk is particularly important for those centers which are not major money centers and affects the regulatory body as well as the center as a whole" (I.O.M. Financial Supervision Commission, 1994a, p. 5).

In addition to an inward-looking focus, many small island financial regulatory bodies link into large supranational institutions as they seek to adhere to global functional standards. For example, the Offshore Group of Banking Supervisors, which was set up in 1990 at the instigation of the Basle Committee on Banking Supervision, now comprises 19 OFC jurisdictions. The purpose of the Offshore Group is to uphold the Basle standards for the supervision of international banking groups. In addition, some OFCs seek to gain membership or "recognition" in other international regulatory bodies such as IOSCO or ECG.

Regulatory challenges are apparent when considering type of offshore financial services offered. Usually, the largest institutional players present in OFCs are banks (Burt, 1995; Hampton, 1994; Johns and Le Marchant, 1993; Roberts, 1994). Offshore banking is inextricably linked to the rise of the Eurocurrency markets beginning in the 1960s (Blum, 1984; Metais, 1990) and more liberal domestic and international legislative changes in the 1980s and beyond (Berger et al., 1995; Borio and Filosa, 1994). The offshore banking sector is facing distinct regulatory challenges as bankers are beginning to realize that the world market for private offshore banking business is changing rapidly, and the banking community will have to be nimble to take advantages of the changes. Quality regulation is needed to attract both banks and quality clients and the regulator should be seen as 'being at the shoulder' of international offshore banking business.

The spatial distribution of OFCs and indeed the global system itself is, therefore, in part conditioned by the regulatory practices which affect those engaged in providing financial services. Of particular importance is the development of comprehensive, accommodating, high-quality modes of financial regulation and supervision. Findings will show that for one OFC (the Isle of Man), creation of this type of regulation occurs through the extensive use of networks. The theory of networks as applied to financial services and regulation is discussed in the next section.

Networks

> Economic space [is] a 'relational' space, the field of social interactions, interpersonal synergies and social collective actions that determine the innovative capability and the economic success of specific local areas (Camagni, 1991, p. 1).
>
> In the spatial sphere, the key elements of the networked region include: a thick layering of public and private industrial support institutions, high-grade labor-market intelligence and associated vocational training, rapid diffusion of technology transfer, a high degree of interfirm networking and, above all, receptive firms well disposed toward innovation (Cooke and Morgan, 1993, p. 562).

The study of networks, whether in the form of Network Analysis (Knocke and Kuklinski, 1991) or development of the Network Paradigm (Cooke and Morgan, 1993) has enjoyed a recent resurgence in the arena of economic geography. Current researchers acknowledge that the roots of the modern network approach lie in the study of business organizations (Cooke and Morgan, 1993; Yeung, 1994). Frances et al. (1991, p.14) assert that "a network is often thought of as a 'flat' organizational form in contrast to the vertically organized hierarchical forms" of market and hierarchy (see Williamson, 1975, 1985).

Furthermore, a rich sociological literature has been used by economic geographers as the building block for a new conceptualization of the way in which businesses are organized (Murdoch, 1995; Powell, 1991; Thorelli, 1986; Yeung, 1994, 1997). The sociological roots of current discourses in economic geography stress the importance of interpersonal relationships as the driving force behind network success (Thompson et al., 1991).

Most applications of the network approach have addressed interfirm networks of production (Christensen et al., 1990) applied to the manufacturing sector of the economy (Cooke, 1996; Malecki and Veldhoen, 1993; Malecki and Tootle, 1996, 1997; Park, 1996). Applications of the network approach to the service sector of the economy stress information and telecommunications networks (Antonelli, 1992), business networks (Perry and Goldfinch, 1996), intrafirm networks (Beyers, 1990), supplier-user networks (Anderson et al., 1990), and local networks (Bennett and McCoshan, 1993). Several types of network may be identified. Rhodes (1991) distinguishes between policy and territorial communities, issue networks, professional networks, intergovernmental networks, and producer networks. Grabher and Stark (1997, p. 534) see networks as the "proper analytic unit" to be used when addressing economic change over time and space.

Powell (1991, p. 272) asserts, "Networks are particularly apt for circumstances in which there is a need for efficient, reliable information." Use of the network approach in research on the geography of finance--where information is critical--has been limited (Leyshon and Thrift, 1997) and no-one has yet applied the network approach to the study of offshore financial centers in the global economy. Specifically, what has yet to be analyzed

is the role played by private-public networks in the creation of spatially focused financial regulation.

Debate exists regarding the true *form* of the network approach as evidenced by Cooke and Morgan's (1993, p. 543) assertion that ". . . the *network paradigm* is not so much a theory as a potentially rich analytical framework for understanding new trends in corporate and spatial development" (original emphasis). In contrast, Yeung (1994, p. 473) argues that the "purpose of network analysis in economic geography is to revitalize the neglected aspects of industrial organization in space." Yeung acknowledges that the notion and meaning of the network *concept* is still ambiguous and offers a more precise definition of a business network as "*an integrated and co-ordinated set of ongoing economic and noneconomic relations embedded within, among and outside business*" (p. 476, original emphasis). Furthermore, according to Yeung, a network should be considered as both a structure *and* a process. In other words it is a dynamic entity concerned with both notions of economic relations and power structures inherent within interpersonal relations and interactions.

The successful functioning of networks, therefore, is conditioned upon the existence of some basic constructs of human behavior, notably: trust and cooperation (Granovetter, 1985; Thompson, 1991; Malecki, 1997a; Yeung, 1994). The importance of "trust" has been recognized as playing an important role in the successful functioning of the modern economy (Gertler, 1988). Park (1996) introduces the notion of spatiality with respect to the construct of trust by arguing that trust can "be built up over a period of time through repeated interactions. Since these repeated interactions are required to build up trust, *geographical proximity* is regarded as an important factor" (p. 487, emphasis added). Trust as a specific

cultural construct has been explored by Mitchell (1995) with specific application to Asian society.

The importance of face-to-face interaction in the provision of financial services is becoming apparent within an international financial system which "has become *more* social, *more* reflexive and *more* interpretive since the breakdown of Bretton Woods" (Leyshon and Thrift, 1997, p. 292). They argue that the new international financial system is best theorized by drawing upon actor-network theory--a postmodem[4] discourse developed by French sociologists Callon (1991), Latour (1993), and Law (1994). Leyshon and Thrift (1997, p. 297) define actor-networks as "actors who are constantly acting through intermediaries--texts, humans, non-humans and money--which are put into circulation in attempts to construct and maintain power relations". Such networks are seen as the "chief structures of govemance in the international financial system, which together constitute the fragmenting 'post-politics' of international money" (ibid, p. 298). This theoretical discourse is abstract and offered at the macro-level. Its contribution to the geography of offshore finance and OFCs lies in the exposition of the organization of money capitalists--one of the four actor-networks which Leyshon and Thrift claim to exist within the international financial system. Leyshon and Thrift argue that the need for *trust and reciprocity* within the organization of

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[4]"Postmodernity" refers to the attempts by social scientists to develop theoretical discourses to understand the "sea-change in cultural as well as in political-economic practices since 1972 . . . which is bound up with the emergence of new dominant ways in which we experience space and time" (Harvey, 1989, p. vii). According to Yapa (1996) it can be thought of both as object or ontology (a *description* of the world) and as epistemology or attitude toward research (*how we know* what we know). See Harvey (1989) and Leyshon and Thrift (1997) for further discussion and analysis of postmodem money.

money capitalists is a critical element in the successful functioning of the international monetary system.

Offshore finance--where the major service provided is management of other peoples' money--is a sector of the economy where the development of *trust* between service provider and consumer, and the existence of cutting-edge *knowledge* of financial products and regulatory constraints on the part of the service producer, are essential to the successful functioning of businesses. A fundamental building block supporting the creation of these necessary constructs is the establishment and maintenance of a superior *reputation* of the offshore center itself (as well as the service provider) in the world of international finance. Because of the rapid increase in the number of OFCs in recent years, offshore financial services providers argue that reputation is place-based as well as institutionally- and individually-based. Some places aim to become known as reputable international financial centers by developing strong regulatory frameworks, recognized as such throughout the world (Burgess, 1997). This usually requires commitment by both the public sector (the government, acting as regulator and supervisor) and the private sector (financial services firms) to work together in a combined effort to promote the OFC. In other words, using Amin and Thrift's (1993) nomenclature, the place must exhibit "institutional thickness" when striving to create trust and reputation, and to share knowledge–so critical the offshore financial services sector–through the successful operation of *networks* of financial services providers and government regulators and supervisors.

Public-private networks or *partnerships* have become an important means of regional economic development in recent years (Bassett, 1996; Bennett and McCoshan, 1993).

Bennett (1996, p. 540) reports that, in an urban context, such partnerships can be seen as a "form of community regeneration more sensitive to the realities of market forces and more in tune with the need to mobilize local communities to compete with other cities for a share of increasingly mobile, global investment". Hastings (1996, p. 259) argues that such partnerships produce *synergy* "in the form of an increased profit for the private-sector participants and in producing new resources to advance the social goals of the public-sector partner".

This research project argues that the successful creation and functioning of local issue-driven networks--public-private, and professional--is a critical element in the success of a small OFC. The successful functioning of these networks is facilitated by the trust that is relatively easy to develop and maintain due to the fact that in these small communities everyone knows everyone else. Bennett and McCoshen (1993, p. 206) argue that the "character of local networks, their leadership and elites, is . . . fundamentally determined by the economic structure and layout of their economies which itself depends on the relation of the local economy to the national and global economic system." Uzzi (1996, p. 675, emphasis added) argues that "the structure and quality of *social ties among firms* shape economic action by creating unique opportunities and access to those opportunities".

In a small island OFC, such ties occur through proximity and are used in the formation of public-private issue-driven networks relating to the creation and maintenance of a superior reputation amongst OFCs. Such partnerships can create *policy synergy* (Hastings, 1996) resulting from the interaction of actors representing the different perspectives of both public and private sectors. As Mizruchi & Galaskiewicz (1994 p. 245)

conclude, ". . . decision making is embedded in social structures, both at the interpersonal and interorganizational level. Administrators and executives are en-meshed in an elaborate network of social relations both within and across organizations." As has already been argued, the creation of a superior reputation by an OFC is necessary for its successful participation in the global economy and it is driven, in part, by the dynamic nature of these issue-driven networks as actors switch roles and positions within the private sector, and--common to the workings of small island OFCs--often switch role *between* private and public sectors.

Summary

The successful growth of an offshore financial center is conditioned upon the development of various links between the local and the global. Conti (1997, p.7) recognizes that "local actors or agents interact globally not only as individuals but also as an expression of the territorialized socio-economic relationships within which they are embedded. At the same time, the same local systems interact with other systems at other levels through the intermediation of the individual agents that belong simultaneously to both local and global networks".

The financial services sector is a piece of the global economy where the creation and maintenance of *trust* is a vital part of the successful functioning of the system. It is argued that the most critical linkage is the creation and subsequent promotion of a superior reputation in the global economy, a reputation as a safe, confidential, and secure place to invest capital. Reputation of an OFC is based upon the creation of a spatially focused

regulatory and supervisory regime with the aim of concurrently exploiting *and* legitimizing regulatory differences to offer advantages to global investors which cannot be found elsewhere.

This research project argues that local-global linkages with respect to regulatory issues are established through the successful functioning of local networks and the existence of what Amin and Thrift (1993) call "institutional thickness." Because of local interaction through inter-firm *and* public-private networking, issues are identified which are critical to the attractiveness of one OFC as compared to others. The willingness of both public and private sectors to work *with* each other in the creation of regulatory-based legislation and the subsequent agreement of the private sector to be monitored *by* the public sector seem to be essential in the establishment of a superior reputation. Further local-global issues are necessary as the OFC has to be seen to be willing to conform to supranational regulatory standards as well as establishing their own regulatory regime. In addition, local-global linkages are developed by both public and private sectors--through the functioning of international business and social networks-- as part of OFC marketing strategies for the place itself and for niche products and services found within. Often, international business, and concomitant social, networks are driven by the migration patterns of skilled labor as they are transferred across the globe as part of career trajectories with transnational banking, accounting, or insurance corporations (Beaverstock, 1991, 1996; Beaverstock & Smith, 1996).

Drawing upon the above theoretical discourse, this paper will develop a conceptual framework in the next chapter to show, first, what combination of place-specific factors

drive the creation and success of an OFC, and second, how the local is linked into the global with respect to the provision of offshore financial services. It will be argued that such local-global links are forged along three dimensions: location, function, and regulation. This framework will be used to analyze the growth of the Manx (Isle of Man's) offshore financial services sector. The Isle of Man is a British Isles' Crown Dependency lying in the middle of the Irish Sea and is one of four major British Isles' offshore centers (the others being Jersey, Guernsey, and Dublin's International Financial Services Center or IFSC).

CHAPTER 3
GROWTH OF AN OFC: CONCEPTUAL FRAMEWORK, RESEARCH METHODOLOGY, AND PRELIMINARY EVIDENCE

Introduction

To successfully participate in the global economy, OFCs (the majority of which are small island economies) have to find ways of successfully and reputably interacting with the rest of the world. The global financial system is predicated upon the relationship between financial institutions, financial instruments, and spatial nodes interacting with the market and operating within the bounds--wholly or partly--of regulation and supervision. Financial institutions comprise a wide range of organizations, including: traditional financial firms such as commercial and investment banks and credit unions; financial companies proving mutual fund services; pension funds; insurance companies; and non-traditional companies such as large manufacturing multi-national corporations (Hirtle, 1993; Lewis and Davis, 1987). Institutions lie (supposedly) totally within the sphere of regulation and supervision in which they are geographically located. As such, they are influenced strongly by the financial and business climate provided by the spatial node. The activities of institutions can in turn influence the success and the reputation of the financial center.

Financial instruments are those things that either: (a) facilitate the exchange of claims of borrowers and lenders, such as a mortgage or car loan, or (b) use financial markets to

increase capital, such as mortgage-backed securities, futures contracts, and hedging strategies. Financial instruments lie both within and outside the sphere of regulation and supervision. The simple exchange of claims between borrowers and lenders falls well within the sphere of regulation, whereas the phenomenal growth of the number and range of derivative instruments over the past decade has surpassed the scope of the existing regulatory and supervisory framework (Kelly, 1995).

Both institutions and instruments have been greatly affected by the increasing use of securitization of, for example, mortgages and other consumer loans. Securitization refers to the transformation of nonmarketable loans into marketable securities (James, 1995; Greenbaum and Thakor, 1995). This implies the creation of a whole new range of instruments and institutions thus adding to the complexity of the financial system. Current research is beginning to address the issue of financial regulation and supervision of this increasingly complex system (Akyuz and Conford, 1995; Gentle and Marshall, 1992; Marshall et al., 1992).

Financial centers comprise the most spatial and "real" element of this increasingly dynamic, complicated and intangible system. These spatial nodes operate within and without the sphere of regulation and supervision due to their dual role as (a) creators and monitors of place-specific regulatory and supervisory regimes and--critically for offshore finance--(b) as active players in the financial marketplace by creating wealth through the facilitation of the appropriate business climate for financial activities to take place. Furthermore, the regulatory and supervisory framework established by specific offshore places can significantly alter the *reputation* of that place in the global economy.

Conceptual Framework

How can an OFC create a superior reputation and become a "successful" participant in the global economy? Previous research indicates that the major factors influencing the growth and development of a small island OFC are:

(1) regulation and supervision

(2) communications technology

(3) networks

(4) labor characteristics

(5) location

(6) political stability (see Figure 3.1).

The major driving force behind the creation of an OFC is the initial development of a "welcoming climate" with respect to regulation and taxation. Such a climate results from a deliberate legislative program to create an accommodating legislative and regulatory regime when compared to the onshore world. Elements of this regime include: low income tax or corporate tax rates; low start-up costs and fees for offshore or non-resident companies; and, more importantly, the ability to instigate proactive rather than reactive legislation in order to exploit a niche market or a niche product.

Fundamental to the continued growth of an OFC is the establishment of a superior reputation in the arena of offshore finance which is based upon the perceived quality of its financial regulatory and supervisory environment. This usually requires commitment by both the public sector (the government, acting as regulator and supervisor) and the private sector

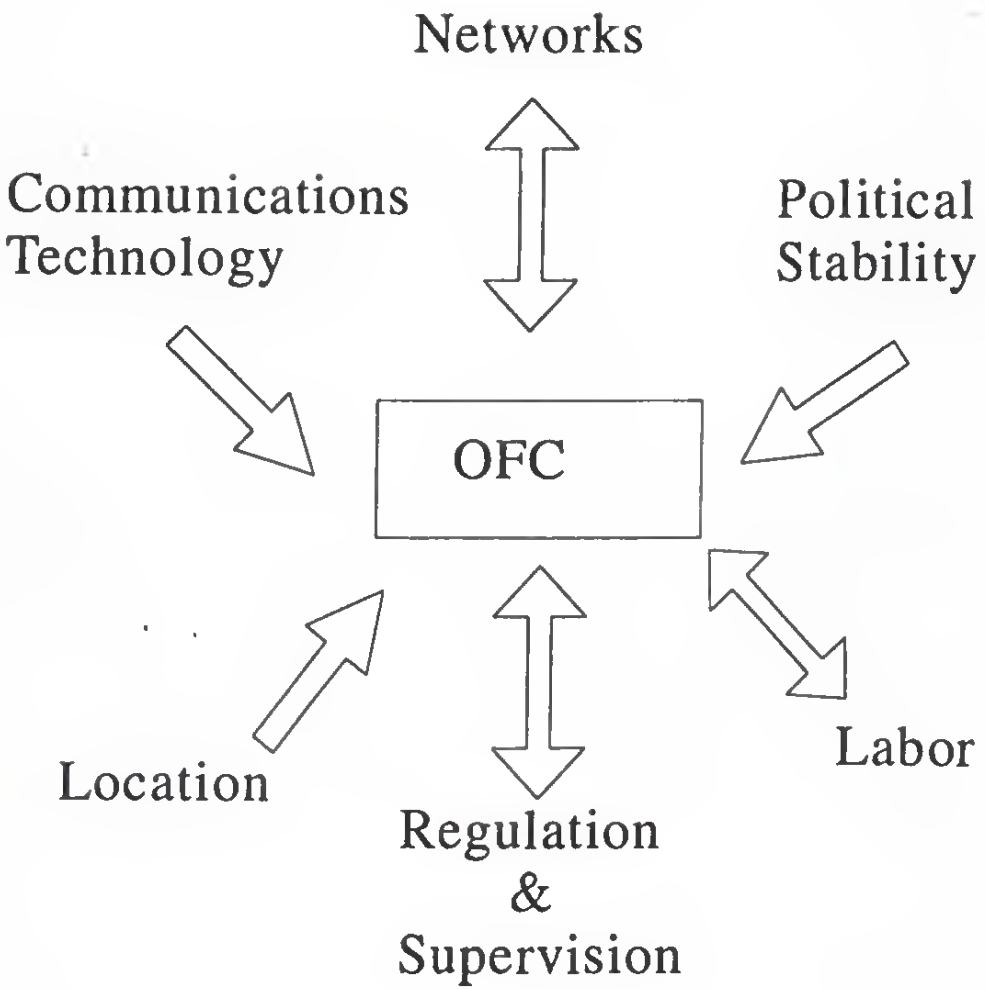

Figure 3.1. Factors influencing the growth of OFCs.

(financial services firms) to work together in a combined effort to promote the OFC. In other words, using Amin and Thrift's (1993) nomenclature, the place must exhibit "institutional thickness" when striving to create trust and a positive reputation, and to share knowledge, so critical to the offshore financial services sector (Thrift, 1994), through the successful operation of *networks* of financial services providers and government regulators and supervisors.

It is accepted by many that the globalization of service industries has been driven by technological change (Malecki, 1997b). Moreover, the provision of global financial services and products is inextricably linked to the availability of high-quality telecommunications services (Hayter, 1993; Gillespie and Williams, 1988; Langdale, 1985, 1989; Moss, 1987; Warf, 1989, 1995). Superior telecommunications services, complemented by quality of life considerations (such as recreational amenities) and good air transportation links for necessary face-to-face linkages, add to the attractiveness of an OFC (Goldberg et al., 1988).

Formal and informal business networks have been shown to be critical to the success of small places and small firms (Malecki and Tootle, 1997; Murdoch, 1995). Rather than facilitate the efficient provision and distribution of tangible products by connecting suppliers and manufacturers (Malecki 1997a), local business networks in the context of offshore financial services play a variety of roles. Both formal and informal networks of actors exist within financial communities (see Thrift, 1994, for the example of the City of London) that are both local *and* global in nature due to the flexible characteristics of the actors themselves. Such networks are used to share information and knowledge about all aspects of the financial system, and market the (intangible) financial products offered by that particular place.

Furthermore, local public-private networks are used to further refine and massage the existing regulatory framework that *allows* particular financial services and products to be marketed in that place. This network role is of critical importance when identifying those offshore places which are successfully and reputably participating in the global economy.

Other global-local linkages may occur through networks that are based upon historical trade or capital flows, for example, an investment bank in a British Isles OFC having traditional links to the Far East may interact with Hong Kong or Singapore on a daily basis. Complementing corporate networks, informal linkages may exist between key individuals working in the financial sector. For example, the migration of a key British expatriate back to a British Isles OFC may well foster specific global linkages within the sector corresponding to that individual's own social and business network and the trust and knowledge that is established within that network over time (Granovetter, 1985).

As the financial system of the 1990s is characterized by its complexity, particularly with respect to new financial instruments used in the marketplace, a well-educated, literate, skilled workforce is a crucial requirement for an offshore center. Particularly important is a pool of highly educated, skilled and relatively mobile professional and managerial workers who are willing to locate to a small place and who then form the core of the business elite (Beaverstock, 1991, 1994). Frequently, such professionals are non-local moving within the corporate network of large financial firms, such as banks or insurance companies, as part of the progression up the corporate ladder. They bring with them new knowledge and insights to the financial sector and serve to diffuse innovative practices and products within the offshore center. Often, the turnover of these upper management professionals is high

resulting in a steady stream of new information to the OFC. In other instances, local actors develop skills and expertise from within and use their local knowledge to complement that of non-local actors.

Location, specifically proximity to a major financial center, is an important element in ensuring the success of an OFC. Proximity may be thought of both in a literal sense (in terms of physical distance and accessibility) and in a figurative sense (in terms of similarity of legal infrastructures and type of law practiced). In the case of the Isle of Man, the Manx legal system is based on the principles of English common law but with important differences: "Manx law has been developed to meet the Island's special circumstances, particularly with regard to direct taxation, company law and financial supervision" (Isle of Man Government, 1996b, p. 6). The judicial system based on English common law which is present in the Isle of Man and most Commonwealth countries is seen as a sign of stability and security and is an attractive force for several OFCs including the Isle of Man, and former British colonial possessions in the Caribbean.

So much is at stake in the workings of the financial marketplace that the political stability of the financial center must never be in question. A well-established democratic system is one of the reasons cited for the success of the British Isles OFCs (Johns and Le Marchant, 1993). Hampton (1996c) has taken the political issue even further, asserting that the political status of an OFC is of paramount importance. "Most OFCs are either dependencies, ex-dependencies or colonies of a major power or are in some form of relationship with a mainland or 'onshore' country" (ibid., p. 69). Hampton further argues that the *attitude* of the onshore state toward the offshore state helps understand the location of

OFCs today. Since the London-based establishment of the Euromarkets in the 1960s, the UK has been known for its more permissive attitude toward OFCs especially when compared to the US. Moreover, "the overall attitude of the UK government towards OFCs appears to have changed over time from acquiescence to encouragement" (ibid., p. 77).

Some of those factors argued to be important to the success of OFCs are more global, controlled and facilitated in part by the nearest financial core, specifically, the factors of legislation, political relationship, and location. The other factors (technology, networks and labor characteristics) are more local and tend to be developed independently by the marketplace and are less influenced by the political relationship between OFC and core. The next section will further develop the conceptual framework by analyzing how the local and global are linked in the workings of an offshore financial center.

Forging Local-Global Links

How does one OFC link into the global economy? Figure 3.2 illustrates the local-global links along three dimensions: location, function, and regulation (see also Cobb, forthcoming). Although reputation, created in most instances through specific financial regulation and supervision, is the most critical element in the successful operation of an OFC, the position (or location) of the OFC, as well as the functional links exhibited by financial firms operating in the center, are essential elements in the analysis of global-local linkages.

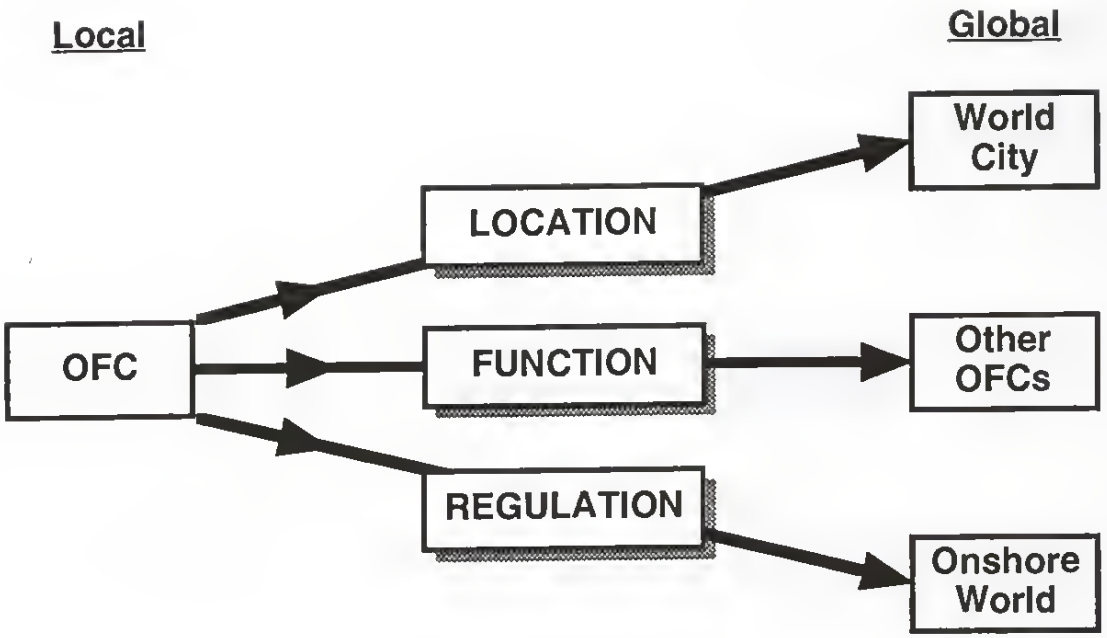

Figure 3.2. Forging local-global linkages

Locational Dimension

Links to the *nearest* world city (London, in the case of the Isle of Man) are stronger than links to other world cities due to proximity and same time zone (this factor was noted by Roberts 1994). Proponents of the view that location no longer matters (O'Brien 1992) have been far outweighed by those who believe that face-to-face interactions will always be important (Granovetter, 1985; Pryke and Lee 1995; Thrift, 1994). Moreover, regular face-to-face contact solidifies both the *trust* that develops between those involved in the provision

and consumption of financial services, and the necessary and often fluid *knowledge* that is required for the successful provision of such services (Leyshon and Thrift, 1997). Much face-to-face contact occurs between an OFC and a world city, on the part of financial services providers, offshore clients, and the OFC government acting as the regulator of such services, so proximity (via an accessible and reliable airline connection) is vital. Regular face-to-face contact serves to deepen the critical construct of trust between offshore service provider and onshore client, and to solidify the necessary flow of information or knowledge between onshore and offshore regulators and legislators.

But the locational or geographic relationship between the OFC and mainland centers is more complex than just a matter of distance. The links between OFC and mainland center has to be seen in terms of the political infrastructure linking (or separating) the two. "Relationships between the dominant blocs and the adjunct offshore financial centers at their margins are contradictory, as the powerful countries treat the offshore centers at once as useful and as an irritating potential threat" (Roberts, 1994, p. 101). The relationship between an OFC and a core financial center may take many different forms. The nearest mainland center may have the power, depending on the political status of the OFC, to curtail OFC access to the global financial system by legislatively "shutting down" offshore operations. In the case of the British Isles' OFCs the relationship may be described as parasitical, as OFCs could not survive without the political consent of the core (London). That relationship is also fragile and vulnerable, in that the dependent political status of the OFC ensures that changes in the political climate of the onshore jurisdiction could have serious ramifications for the OFC. The relationship between non-dependent territories (for example Cyprus or

Barbados) and their respective financial cores may be less overt and the political will of the core be felt less keenly in the OFC.

Functional Dimension

The functional fit, expressed in terms of the organizational relationships between financial services providers in an OFC, on the one hand, and international markets, head offices, other financial companies and international investors, on the other, is another way to conceptualize global-local links. Spatially, this is particularly evident in the way in which one OFC is in regular contact with other OFCs because of the functional networks established by service providers. Formal linkages are normally present within the corporate structure of many of the financial institutions present on an OFC, for example, the distribution of branches of a global banking network or insurance firm. Within the past year, many global offshore banking facilities in the British Isles' OFCs (for example, offshore operations of some of the major high street banks, along with some of the older investment houses), have reorganized provision of services within a functional offshore grouping which typically includes all the British OFCs (Jersey, Guernsey, Isle of Man). In other words, all offshore services whether provided and managed from Jersey, or the Isle of Man, are part of the same corporate group. In some instances it is possible to recognize distinct spatial divisions of labor within a particular corporation as front office functions are provided in one OFC and back office functions in another.

Regulatory Dimension

Kleinfeld (1994, p.20) argues that when prospective offshore clients compare jurisdictions, the most important factor is the "legal and regulatory environment which has been specifically established to benefit the type of business being considered or sought". Fisher (1994, p. 19) identifies one of the major OFC success factors as "quality of regulation—a center should be capable of maintaining high standards of regulation combined with a flexible approach . . . it should be easy to use not to abuse".

An OFC is in regular contact with much of the rest of the global economy (the onshore world) in its quest for acceptance and recognition as a reputable place to do business. The legislative "climate" of an OFC specifically with respect to regulation and taxation issues is of fundamental importance to its initial establishment (Doggart 1979; Walter 1985). Furthermore, deliberate public and private marketing and promotion efforts are necessary to see continued growth and success. For example, the government of a small OFC may deliberately target specific financial institutions by passing a piece of legislation, or a specific geographic market by writing legislation, that legitimately meets the needs of wealthy onshore clients in their quest for efficient wealth management strategies.

Research Methodology

No doubt exists as to the complexity of the modern financial system and the existence of three primary financial centers. It has been argued, however, that small island OFCs have a small, but nevertheless important, role to play in the global circulation of capital. But what makes a small island OFC tick? What are these OFCs doing to ensure their continued

success and growth? How exactly do they link in to the global system of capital flows? This section addresses a research methodology to be used to analyze one OFC, the Isle of Man.

The major research questions to be addressed in this project are:

1. *Why has the Manx financial sector grown so rapidly over the past 20 years?*
2. *What type of niche market (if any) and core competencies does it offer?*
3. *How does the island's financial sector link in to the global financial network?*

Primary Data

Primary data were obtained using a personal interview/questionnaire technique, in part because of the author's links to the island as a native, and the fact that representatives of some of the firms are known personally to the author. More importantly, this technique has been used with considerable success by other researchers (see Healy and Rawlinson, 1993; Malecki and Veldhoen, 1993; Markusen, 1994; Schoenberger, 1991; Yeung, 1995).

Approximately 300 firms offering financial services are located on the Isle of Man (Isle of Man Government Finance Factfile, 1995). A stratified sample of 25 percent (≈75 firms) of the total number of firms was drawn to ensure that firms from all parts of the financial sector were included. Specifically, weighted random samples were drawn to ensure inclusion of the following types of firms: banks; investment businesses; collective investment schemes; building societies; insurance companies; shipmanagement companies; stockbrokers; accountants. Representatives of the Manx Government, the Financial Supervision Commission, the Insurance Authority, and other "key players" in the finance sector were also interviewed for further insight on the evolution of regulation and supervision

on the island. Finally, a representative from Manx Telecom was interviewed to gain further knowledge of the role of telecommunications both in the growth of the financial sector and the facilitation of global linkages.

The survey was a mixture of objective and subjective questions (Beaverstock, 1994; Healy and Rawlinson, 1993), and was divided into three sections. Section One of the questionnaire addressed general information about the firm being surveyed. The most critical questions asked in this section pertain to the *size* of the firm, the *type* of services provided, the *ownership structure* of the firm, the *length of time* the firm has been present on the island, and the *growth* in size of the firm since its inception.

Section Two addressed the number and type of *linkages* established by the firm on a daily basis, both external to the island and internal to the island. *Types* of communication link used, *purposes* of communication link, and specific *places* contacted was ascertained. Also, the identification of any formal and informal business *networks* used by each firm was obtained.

Section Three addressed, with subjective, open-ended questions, *perceptions* regarding the reasons for the establishment/growth of each firm surveyed and also the growth of the Manx financial sector in general. Questions addressed the importance of the six major success factors: regulation/ supervision, communications technology, networks, labor characteristics, location, political stability (Figure 3.1).

Secondary Data

Secondary data were compiled both to compare with, and expand, the findings from the primary data. Secondary data were gathered to ascertain the exact quantitative growth of the sector over the past twenty years, coinciding with the First Banking Act of 1975 (I.O.M. Financial Supervision Commission, 1994a). The data were compiled from a variety of sources including: I.O.M. Census, I.O.M. Govemment Policy Reports, *I.O.M. Government Industrial, Financial and Commercial Directory,* I.O.M. Financial Supervision Commission Annual Reports, telephone directory yellow pages, *Isle of Man Examiner.*

Secondary data addressing legislative changes made over the past twenty years were compiled from Isle of Man Govemment Policy reports and information available from the Isle of Man Govemment Office of the General Registry. Specific legislative changes (Acts of Tynwald) were compared temporally to the growth in the number of financial institutions operating on the island. Data addressing specific changes in the telecommunications industry over the past twenty years were obtained from Manx Telecom.

Data Analysis

Chapters 4, 5, and 6 analyze the results of the survey/questionnaire given to financial practitioners and government officials. Findings will show that responses to all questions vary by type of service provided by the firm:

1. *Banks* are likely to: be branches of intemational firms; have been on the island for a relatively long time; have been influenced by the Banking Acts 1975-86; have

benefitted from the establishment of the Financial Supervision Commission in 1983; make large numbers of external linkages using private, sophisticated communications networks centered on London; have the need for a relatively large number of skilled and semi-skilled workers.

2. *Investment Businesses* and *Collective Investment Scheme Managers* are likely to: be newer additions to the island's financial sector having responded to specific legislation and supervisory practices established in the late 1980s; have less sophisticated modes of communication; have mainly U.K. rather than global linkages; require a skilled labor force.

3. *Building Societies* are relative newcomers to the island, due to the passage of the Building Societies Act of 1986, and are likely to: have most linkages with the U.K.; require both skilled and semi-skilled workers; believe location is a critical factor.

4. *Insurance Companies* are likely to: have seen the greatest amount of growth after the passage of the Insurance Act of 1986; contain a mix of global and local firms with associated differences in mode of operation; require skilled and semi-skilled workers.

5. *Shipmanagement Companies* are likely to: vary in size; have mostly global linkages; require skilled and semi-skilled workers.

6. *Stockbrokers* and *Accounting Firms* are likely to: vary in size and ownership structure; require a relatively large number of workers with professional qualifications; vary in type of linkages but focus on London; use and benefit from business networks.

In general, it is expected that the six so-called success factors will vary in importance according to the type of services provided by the firm. It is likely, though, that regulation/supervision and formal and informal networks will be critical factors for every firm. The importance of technology will vary according to size of firm and type of service provided. All firms have certain labor characteristics in common, i.e., the demand for skilled labor, but the mix of skilled/semi-skilled labor will vary by size of firm and type of service provided. The factor of location will vary in importance depending on type of service provided and niche market served. The political stability of the island and its political relationship with the U.K. will be important, but not critically so, to all firms.

Setting the Stage: The Isle of Man as an OFC

The Isle of Man is a British self-governing Crown Dependency located mid-way between England and Ireland in the Irish Sea (Figure 1.1). The land area of approximately 220 square miles contains a population of over 71,700 in 1996 which is the highest population recorded since the Census was first undertaken in 1821. The Manx economy is now dominated by the finance sector, which has doubled in importance over the past twenty years to comprise 36% of the island's GNP and almost 20% of the workforce (Lapper and Stuart, 1996). The Isle of Man lagged behind the Channel Islands (Jersey and Guernsey) which began to function as OFCs in the 1950s and 1960s) in its quest to become a diversified, international OFC (Hampton, 1996b). However, the importance of the Manx offshore financial sector has been evolving slowly over the past 30 years, beginning with the deliberate effort by the government in the early 1960s to establish the island as a "tax haven"

for high net worth individuals (HNWI). These HNWI were attracted to the island because of the development of a favorable income tax regime created by abolishing the island's surtax and reducing the standard rate of income tax (Solly, 1983), and a concomitant punishing tax regime (as perceived by many British HNWI) existing in 1960s Britain under the Labour Party government.

The island enjoys total independence from the UK on matters of direct taxation. Features of the tax system include low corporate and personal tax rates, no capital transfer or gifts tax, no capital gains tax, and no death or estate duties. Although not full members, the Island, along with Jersey and Guernsey, has a special relationship with the European Union (EU) under Protocol 3 of the Act of Accession of the UK and is required to apply the Common Customs Tariff and equivalent measures to those operated by the UK under the Common Agricultural Policy. This relationship allows for free movement of goods between the Island and the EU whilst at the same time releasing the Island from compliance with all of the other bureaucratic regulations regarding the marketplace. This special relationship with the EU might be perceived as an extra factor conditioning the growth of the island as an OFC as "outsiders" are able to gain access to the EU through the island. Furthermore, the island is considered outside the Union for trade in financial services and products, and is not therefore bound by Union directives in this area (I.O.M. Financial Supervision Commission, 1994a).

With the aim of further developing and broadening the island's financial services industry, two significant pieces of legislation were enacted by Tynwald (the Manx Parliament) in the 1970s: the Companies Act of 1974, and the Banking Act of 1975. The

former served to authorize insurance companies carrying out business in the island, and the latter provided for the licensing of banks and certain investment businesses in the island. What was lacking at this point, though, was effective regulation and *supervision* of businesses once authorized or licensed. Furthermore, the lax regulatory regime enabled a series of business failures to occur in the early 1980s—in particular, the devastating crash of the Savings and Investment Bank Limited (SIB) in 1982, with the loss of a deposit base of over £40 million, which was attributed to lax regulation and nonexistent supervision. As reported by Solly (1994, p. 90), "the reverberations of these failures continued throughout the decade of the nineteen-eighties. The cost of damage in terms of loss of reputation, loss of confidence, both locally and elsewhere, and the additional expenditures incurred in the winding up, reporting, and various civil and criminal legal actions and, finally, compensation to depositors, is incalculable".

The Manx Government instigated reactive legislation to establish a comprehensive regulatory and supervisory regime to ensure that an "SIB" would never occur again. To this end, the Financial Supervision Commission (FSC) was established in 1983, and the Insurance Authority in 1986. Since the respective dates of their inception, these two Statutory Boards have introduced proactive regulation in the form of "meaningful systems of licensing and supervision of banks, building societies, investment businesses, collective investment schemes [mutual funds or unit trusts] and insurance companies" (Solly, 1994, p. 90). Attraction of offshore business entities, such as non-resident companies, offshore banks, exempt insurance companies and unit trusts (mutual funds), occurs through exemption from Manx income tax. Non-resident companies are particularly attractive to an OFC because of

the fees (in the form of an annual license) they generate. In addition, the island is attractive to those wishing to form non-resident companies because of the low labor costs involved.

The most recent legislative agenda of the Manx Government has been of a more proactive nature whereby *sophisticated regulatory massage* of already existing onshore legislation has resulted in the promulgation of new laws designed to attract international investors seeking to minimize tax obligations within a clear legal corporate entity. This is best exemplified by the Isle of Man's Limited Liability Company Legislation (LLC) based upon the U.S. "Wyoming Principle", which came into force in October, 1996.

Table 3.1 shows the number of firms providing specific financial services in the Isle of Man in 1995. Currently, the deposit base for Manx licensed banks is over £14 billion, up from £2.5 billion 10 years ago; the number of collective investment schemes managed in the island is now well over 100, with assets of over £1 billion; the assets managed by insurance companies stands at over £4 billion; and the number of companies registered in the island is over 36,000 (*Offshore Outlook* 1996; Isle of Man Government 1996).

The financial services sector is a diversified one with similar numbers of banking establishments; insurance companies and brokers; and accountants. In fiscal year 1994/95, the Manx financial sector generated 36% of the island's GDP of £612 million (Isle of Man Government, 1996).

One of the most critical global-local links with respect to regulation is the island's membership (along with 18 other OFCs) in the Offshore Group of Banking Supervisors, which was set up in 1990 at the instigation of the Basle Committee on Banking Supervision.

According to the I.O.M. FSC (1994b, p. 5),

> The Offshore Group supports the Basle Committee's minimum stands for the supervision of international banking groups and their cross-border establishments; and the Basle Committee's Capital Convergence proposals. The Group is also committed to the Basle Committee's recommendations and to the International Financial Action Task Force recommendations on money laundering.

Table 3.1. Financial services firms, 1995

TYPE OF FIRM	NUMBER
Bank (domestic, offshore, building society)	60
Insurance Companies - Life	14
Insurance Companies - Other	22
Independent Insurance Brokers	24
Investment Businesses	46
Fund Management Companies	20
Stockbrokers	6
Accountants	64 (5)
Advocates (Lawyers)	21 (20)
Legal Practitioners	12
Ship management	20
TOTAL	**309**

Source: Compiled from I.O.M. Government Finance Factfile, 1995.
Note: figures in parentheses show number of firms designated as "regulated persons", that is, allowed to conduct investment business.

In addition to adherence to international standards, all banks operating in the Isle of Man have to be granted a license by the FSC and have to conform to issues of both financial and non-financial regulation. Financial regulation covers capital adequacy, prudential ratios, audit, and disclosure requirements, whereas non-financial regulation deals with matters such as ownership, management and conduct of the business. The mechanism which the FSC has chosen to use to minimize reputational risk is a "firmly applied and clearly defined licensing

policy. [Also] the Commission has also always been of the view that it should not license any institution or business which it cannot effectively supervise.....Hence, one of the basic requirements is that applicants should be managed and controlled *on the island*" (I.O.M. FSC 1994a, p. 8, emphasis added). The FSC uses an initial "fit and proper" test which addresses the applicant's satisfaction of three broad criteria: integrity, solvency, and competence. In addition, "in the conduct of banking business a key requirement is the business must be conducted on a day to day basis by at least two individuals (known as the 'four-eyes principle')" (ibid).

The other major statutory body in the island is the Insurance Authority, which functions to implement the Insurance Act, 1986, which is "designed to ensure that those who run insurance businesses are fit and proper and that the companies have sufficient resources at all times" (I.O.M. Insurance Authority, 1996). The Authority authorizes and supervises firms that wish to offer insurance services and also issues permits and registers all insurance management companies doing business in the island. Global-local links for regulation are forged by regulation of Manx-based insurance providers by the International Association of Insurance Supervisors (IAIS) as well as the Isle of Man Insurance Authority.

Further functional and regulatory linkages are forged through membership of Manx regulators in the International Organization of Security Commissions (IOSCO) for international securities transactions, and recognition of the Manx regulators by the Enlarged Contact Group (ECG) which is a global regulator of collective investment schemes (mutual funds/unit trusts) and their operators. The rational for the Manx, and other small island financial regulatory bodies, to link into global supranational regulatory and supervisory

bodies is two-fold: first, to increase the reputation of the OFC as that OFC seeks to adhere to global standards and, second, to benefit from flows of information regarding global financial issues particularly with respect to anti-money laundering policies.

In addition to establishing global linkages, the Isle of Man seeks to benefit from the trust, knowledge, and networks inherent in a small place when creating new, and in many instances proactive, regulation and legislation. The creation of new financial legislation occurs though a process of *consultative committee networking* (Moran's (1991) "Meso-corporatism") whereby representatives of various elements of the private sector (banking, insurance, mutual finds, lawyers, accountants) meet with members of the government (the Treasury, banking and insurance regulator and supervisors) on a regular quarterly basis to address problems and issues of concem. Members of both the private and public sector can place issues on the agenda and free-flowing discourse is encouraged. In many instances, the end result of the consultative committee process is a new piece of financial legislation for the island, often created proactively to exploit niche markets in the burgeoning onshore demand for wealth management strategies. This process, and other networking strategies, is analyzed in further detail in Chapters 4, 5, and 6.

CHAPTER 4
THE GROWTH OF OFFSHORE FINANCE IN THE ISLE OF MAN

Introduction

Perspectives regarding the growth of the Isle of Man as an international offshore financial center, from those actively involved in the provision of financial services on the island, were gathered via a series of personal interviews. A sample of 20 percent of all those engaged in providing financial services was drawn from information published by the Isle of Man Government Finance Factfile (1995), and the Financial Supervision Commission's Annual Report (1995), together listing all practitioners in the sector. The resulting sample size was 68 private sector firms, ranging from banks and building societies, to life and captive insurance firms, to company and trust formation and administration firms, to accountants, lawyers, ship management firms, and others. The final completed sample size was 60 (or 88% response rate), due to the refusal of some firms to participate in the study, and the doubling-up[1] of listings from government sources. The private sector sample was complemented by a survey of 11 representatives within the public sector, in order to capture the difference in perspectives (if any) from the different sides of the financial services sector

[1]"Doubling up" refers to the fact that one organization might actually be listed in government documents as two different companies providing different services and having different financial licenses. The personnel involved in providing the services for the two companies are actually identical though.

itself. One difference which soon became apparent during the survey was the perceived role played by each side in marketing and promoting the island as an OFC. Many of the private sector respondents felt that they alone were responsible for promoting the island until very recently, whereas the public sector respondents had a much more positive outlook on their marketing role. The issue of marketing and promotion of the island is analyzed in much greater detail in Chapter 6.

Data Collection Process

The period of data collection lasted for approximately two and one-half months during the summer of 1996. Representatives from those firms appearing in the original sample population were sent letters of introduction one week prior to my arrival in the Isle of Man, briefly describing the research project and requesting their help. Effort was made to contact the top executive in each firm: some of these names were available from government publications; others were found through inspection of recent business sections of the local newspaper; some were known through links to the island as a native; and a small number were ascertained by telephone calls to receptionists of the firms themselves.

First, potential respondents were contacted by telephone as a means of identifying myself[2], once again asking for their cooperation, and requesting an appointment for an interview to take place. Second, a pilot study was undertaken to test the effectiveness and appropriateness of the questionnaire (see Appendix A for a copy of the questionnaire).

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[2]In a small place like the Isle of Man, receipt of an "official" letter from the United States resulted in almost immediate recognition of my name when first phoning, even by some of the larger firms surveyed.

The actual interview period lasted for 9 weeks and the number of interviews per week ranged from 4 to 13, with an average of 8 per week. Summer months were expected to be "slower" in terms of business activities because of holiday time and some interviews had to be arranged in between executives' off-island holidays[3].

It was not possible to schedule more than 4 interviews a day due to the projected length of each and the time taken to review and write up notes taken after each interview (Yeung, 1995; Markusen, 1994). The business culture of the island (corresponding with the UK and unlike that of the US) results in a working day from 9am to 5:30pm[4]. Most respondents did not want to schedule an appointment "first thing" in the morning or last thing at night, so the effective window for interviewing lasted from 10am to 4pm. The interviews were semi-structured with a number of both closed-end objective questions and open-ended subjective questions.

The private sector interviews ranged from 20 minutes to 2 hours, although on average the interviews took between 45 and 60 minutes. The private sector questionnaires (n = 60) were structured in a different way from the public sector questionnaires (n = 11). Key public sector participants were selected when the survey of the private sector was already underway and the construction of the questionnaire for the public sector was influenced by continuing

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[3]Deliberate planning to conduct the interviews in early to mid-summer rather than late summer resulted in less disruption for respondents' holiday plans. British (and Manx) schools traditionally break for summer holidays from mid-July to late-August or early September which is when the majority of business people also take holidays.

[4]However, a small number of firms (particularly the larger corporations) had extended working hours to correspond with their corporate linkages to offices in other time zones.

feedback from the private sector. The public sector questionnaires, although based on the private sector questionnaire, consisted of a number of additional open-ended subjective questions addressing the reasons for the growth of the Manx financial sector, and the perceived role played by the public sector.

The quality of the information gathered during the interviews varied somewhat: all respondents were polite and most were interested in receiving feedback from the study[5]. As expected, public sector respondents were very enthusiastic about their role in the development of the financial sector and were interested in promoting the island as much as possible. Furthermore, some private sector respondents were genuinely interested in the "big picture" of offshore finance and offered unsolicited opinions on issues not covered in their questionnaire. These open-ended subjective comments are analyzed further in Chapter 5.

Findings

This section presents findings from the objective sections of the questionnaire given to the private sector participants (see Appendix C for aggregate summaries of findings). Most of the open-ended questions including all public sector findings is analyzed in Chapters 5 and 6. The presentation and discussion of data is organized to correspond with the format of the questionnaire. First, general findings illustrating the growth of the finance sector are presented. Second, local-global linkages will be explored and, third, specific linkages in the form of networks is analyzed.

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[5]All survey respondents were promised a summary report of findings which was mailed to them in January, 1997. See Appendix B for a copy of this report.

Type of Service Provided

Of the 60 private sector interviews, 9 (or 15 percent) of the respondents did not provide any type of "offshore" services and are henceforth referred to as the providers of "domestic" financial services. The remaining 51 (or 85 percent) of respondents provide offshore services to non-residents of the Isle of Man and services to high net worth individuals (HNWI) resident in the island; 25 firms also provide domestic services to other firms or services to non-HNWI resident in the island (Table 4.1).

Table 4.1. Type of survey respondents

SURVEY RESPONDENTS	NUMBER	%
Private Sector - Offshore only	26	37
Private Sector - Offshore & Domestic	25	35
Private Sector - Domestic only	9	13
Other[a]	11	15
TOTAL	71	100

Source: author's survey
Note: [a] government officials, regulators, Chamber of Commerce, Manx Telecom.

Findings from the private sector were grouped by distinct financial services sector into 4 categories: banking, insurance, accountancy, and "other". The banking sector includes retail or "high-street" banks, investment banks, and building societies. The insurance sector comprises life assurance (insurance) companies, captive insurance companies, insurance brokers, and individual insurance agents. The "other" sector includes

company and trust formation and administration firms, law firms, investment companies, and shipmanagement companies. Table 4.2 shows that these groups are roughly equal in size and so illustrates that a balanced sample of firms was identified.

Table 4.2. Respondents by Sector

SECTOR	FIRMS	%
Banking	15	25
Insurance	14	23
Accountancy	12	20
Other	19	32
TOTAL	60	100

Source: Author's survey

Figure 4.1 shows the type of financial services offered within each sector. It can be seen that 6 banks provide only offshore services (therefore cannot be used by Isle of Man residents) and 9 banks offer both domestic (retail) and offshore services. Nine insurance companies are offshore only, and 5 provide only domestic services. Nine accountancy firms provide both domestic and offshore services and 3 businesses service only the domestic market. Twelve "other" firms provide only offshore services, 6 firms provide both, and 1 firm serves only domestic clients

Each respondent was asked to provide a more detailed list of the financial services undertaken by that company (Table 4.3).

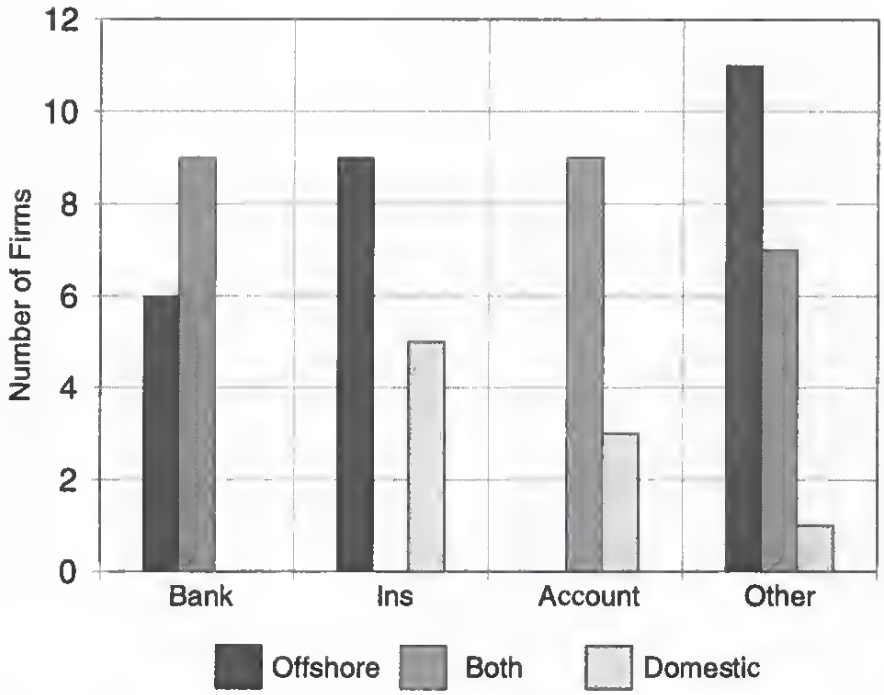

Figure 4.1. Type of financial services offered in each sector.

Table 4.3. Specific services provided by firms.

SERVICE	# FIRMS	% (n =60)
Retail/domestic banking	7	12
Offshore banking	16	27
Accountancy - domestic	12	20
Accountancy - offshore	9	15
Fund management	5	8
Company/trust formation & admin.	11	18
Insurance - captive	4	7
Insurance - life/broking	12	20
Shipmanagement	4	7
Legal	5	8
TOTAL	85	

Source: Author's survey.

The total number of services (85) is greater than the total number of firms (60) because some firms offer more than one type of service. In particular, some of the larger institutions offer a wide variety of services, for example banking, fund management, and insurance services provided by one firm. This is a key finding as current literature acknowledges the increasing trend of "one-stop shopping" for financial services (*The Economist,* 1997b). Financial services provision is further complicated by the fact that different types of firms offer the same type of financial services, for example, company/trust formation services are provided by accountancy firms, banks, investment companies, and advocates (lawyers).

The difference between producer services and consumer services is highlighted by the functional roles of accounting firms. Some provide "domestic" (producer) services which either (a) service the financial sector (for example, audit services for banks), or (b) service the rest of the Manx economy (for example, audit services for manufacturing firms, retailers, farmers, etc.). Others provide direct offshore financial services to expatriate clients and HNWIs living in the island and are competing directly with other offshore financial institutions in the Manx financial sector.

The Growth of the Manx Financial Sector

Growth of the Manx financial services sector is illustrated by: the number of years each firm has been present in the island and the number of employees in each firm. Table 4.4 shows descriptive statistics for the first variable "years". The mean number of years all

firms have been present in the island is 29.1, the standard deviation is 41.1, and the median is 10 years. Chi-squared testing of normality of this variable resulted in the rejection of the null hypothesis at the 0.05 level and therefore precludes any further rigorous statistical testing.

Table 4.4. Descriptive statistics for the variable "Years".

TYPE OF SERVICE	N	mean	s.d.	median
All[a]	60	29.1	41.1	10
Offshore	26	9.0[b]	3.6	9
Domestic	9	46.6	53.9	9
Both	25	43.7	48.9	22
Banking	15	26.6	36.8	16
Insurance	14	33.6	46.6	10
Accountancy	12	28.5	39.8	9
Other	19	28.1	40.6	10

Source: Author's survey.
Note: [a] reject H_o: normal distribution (0.05 level).
[b] significantly different from Domestic & Both at 0.05 level.

The recent vibrancy of the island's finance sector is better illustrated by Figures 4.2, 4.3, and 4.4, which show the number of years firms have been doing business in the island. Over half of the firms are less than 11 years old and more than three-quarters are less than 25 years old. A handful of firms have been present on the island for over 100 years; they served the domestic market until recently, but now some of them have adapted to provide

offshore services in addition to domestic services although, some have not. Some of the smaller firms are new but some or all of their *personnel* have been on the island working in the financial sector for longer, but with a different firm, usually in the accountancy field.

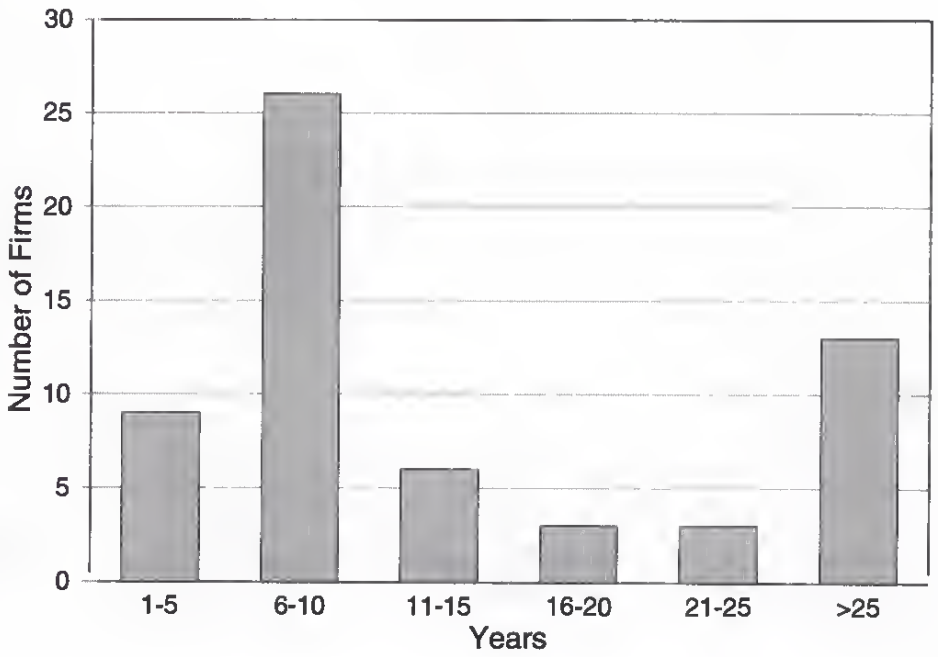

Figure 4.2. Number of years present in the island.

Figure 4.3 shows the length of time on the island by sector and shows that a large number of insurance and "other" businesses commenced operation between 6 and 10 years ago. This can be directly linked to the creation of specific legislation in 1986 (The Insurance Act), which regulates those carrying on insurance business in the island (Solly, 1994). The newest banking sector firms are actually building societies, established in Douglas after appropriate legislation opened the door for their presence in the island (The Building

Societies Act of 1986). The relationship between U.K. legislation and Manx legislation for some building societies in the island may be seen as a process by which the U.K. established "enabling" legislation and the Isle of Man "sympathetic" legislation.

Some representatives of each of the service sectors have been present on the island for over 25 years (some, in fact, for over 100 years) serving the domestic market. Regular and stable growth of banking institutions is evident from inspection of Figure 4.3; most of the growth in insurance companies has been within the last 15 years; and "other" businesses--specifically investment businesses and shipmanagement companies--have seen large growth over the past 10 years. Once again it was the passage of "enabling" legislation that caused this growth to take place.

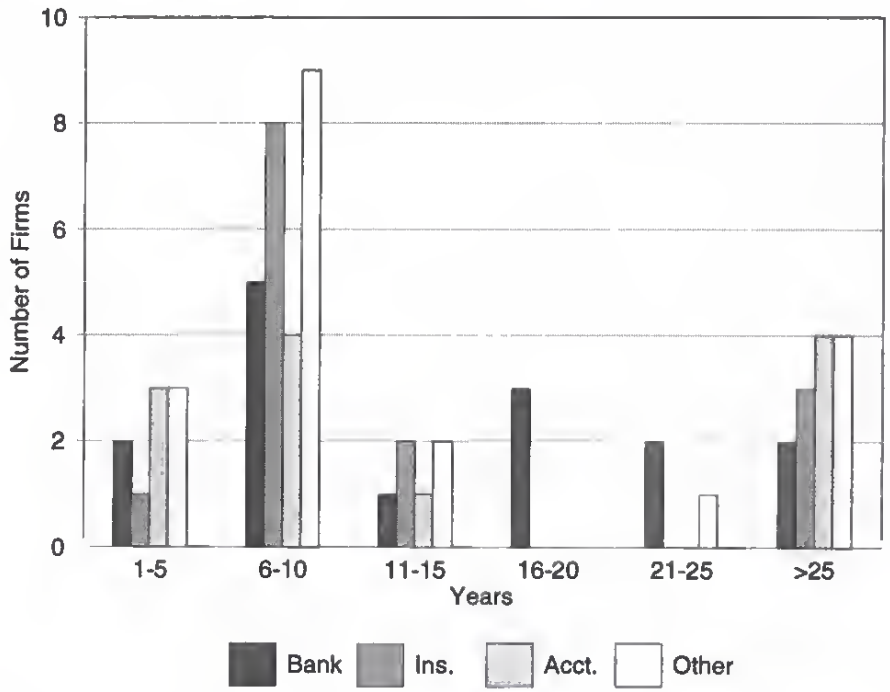

Figure 4.3. Number of years present in the island, by service sector.

Figure 4.4 shows the length of time present in the island by type of services offered (domestic or offshore). It can be clearly seen that most of the offshore growth has taken place over the past 10 years. Furthermore, the largest number of firms offering both offshore and domestic services have been present in the island either for a long time (over 25 years), or over the past 10 years. Few firms have been resident for an intermediate length of time in the island.

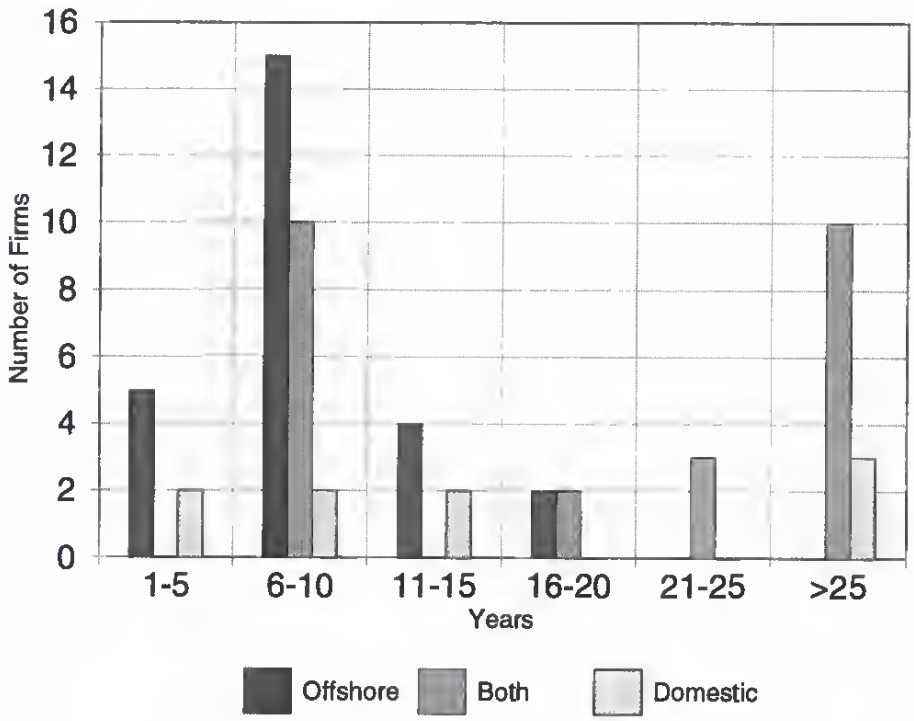

Figure 4.4. Number of years present in the island by type of service offered.

The other variable illustrating the growth of the sector is "employment" which refers to the number of full-time employees within each firm surveyed. Table 4.5 shows the descriptive statistics for this variable which *is* normally distributed at the 0.05 level. The

mean number of employees for all firms is 54.6, the standard deviation is 85.1, and the median is 21.5. These statistics confirm the existence of a handful of firms employing large numbers of people. In many instances, the number of employees grew from small to large in a relatively short period of time, as offices were opened up by one or two individuals who then oversaw a rapid increase in the number of employees as the volume of business grew.

Table 4.5. Descriptive statistics for the variable "Employment".

TYPE OF SERVICE	n	mean	s.d.	median
All[a]	60	54.6	85.1	21.5
Offshore	26	46.2	55.7	20.5
Domestic	9	4.8[b]	4.0	2.0
Both	25	85.9	116.6	39.5
Banking	15	98.2[c]	122.9	39.0
Insurance	14	46.6	67.2	11.0
Accountancy	12	22.0	22.4	12.5
Other	19	46.5	70.9	30.0

Source: author's survey.

Note: [a] accept H_o: normal distribution (0.05 level).

[b] significantly different from Offshore and Both at 0.05 level.

[c] significantly different from Insurance and Accountancy at 0.05 level.

Figure 4.5 shows a breakdown of survey respondents in terms of size of firm. A fairly even distribution in firm size is found, ranging from one-employee operations to firms employing over 200 people. This measure can be used as a crude surrogate for size of business; most small firms are engaged in the provision of domestic producer services

whereas many large firms are part of a national, if not international, business organization. In some instances small firms were established as "spin-offs" from larger organizations. A typical example of this process occurs within the accountancy sector, where an individual will have trained and obtained the necessary professional qualifications while employed at a large firm, then subsequently leave to set up a small-scale independent operation with one or two employees, in some cases servicing the financial sector (producer services) and, in others, directly competing with other firms providing offshore (consumer) services. This trend was noted by Daniels (1995).

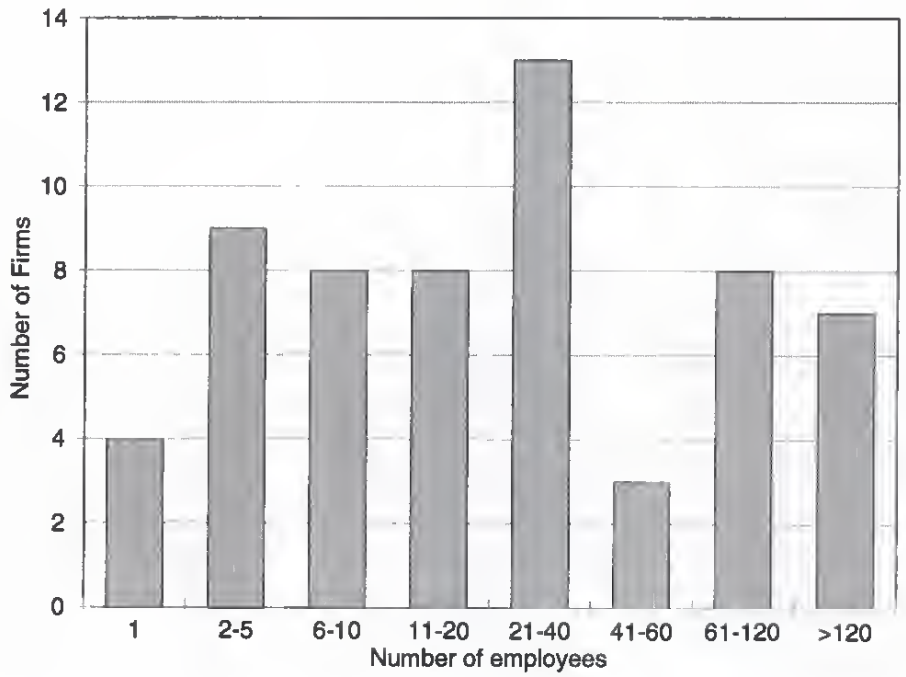

Figure 4.5. Firm size.

Firm size within the four specific financial sectors is shown in Figure 4.6. The greatest range in employee size occurs within the insurance sector range from one-person businesses to very large firms of over 120 employees. Banks and "other" range in size from very small (2-5 employees) to very large (greater than 120 employees); accountancy firms range from very small to moderately large. Banking and accountancy are significantly different from each other at the 0.05 level as are banking and insurance. Furthermore, firms offering domestic services only are significantly different from those offering offshore services and both types of services (Table 4.4). These findings illustrate that the Manx financial sector is diversified in both *type* of financial service offered and *size* of firm.

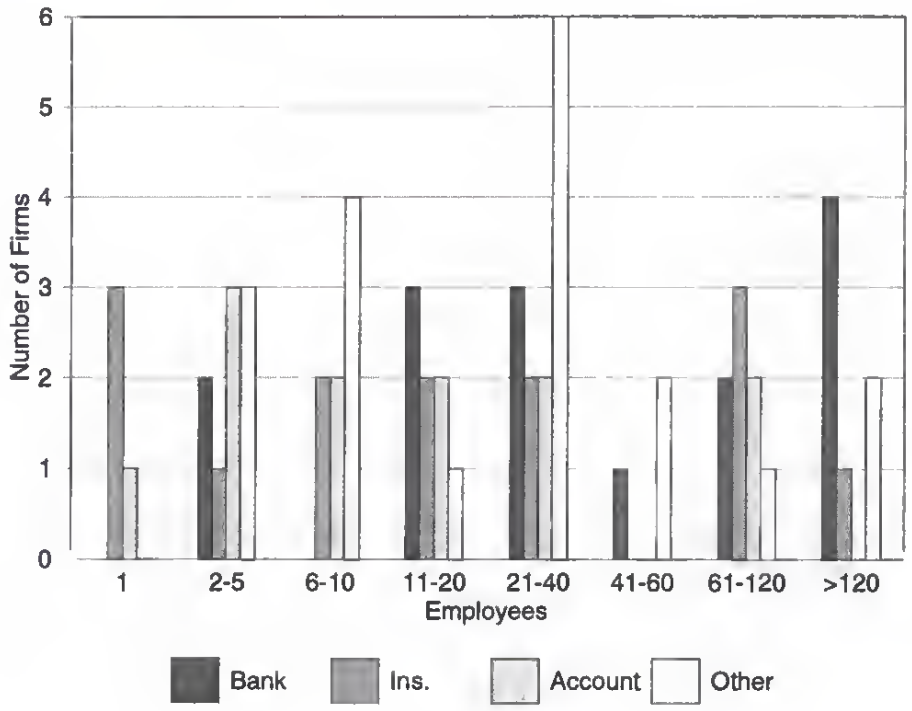

Figure 4.6. Firm size by service sector.

Figure 4.7 shows firm size by type of service offered. Those firms providing offshore services only have a wide variety in size, as do those providing both services, ranging from small to large. Those firms providing domestic services only are not larger than 10 employees, and are significantly different from the other two services at the 0.05 level (Table 4.5).

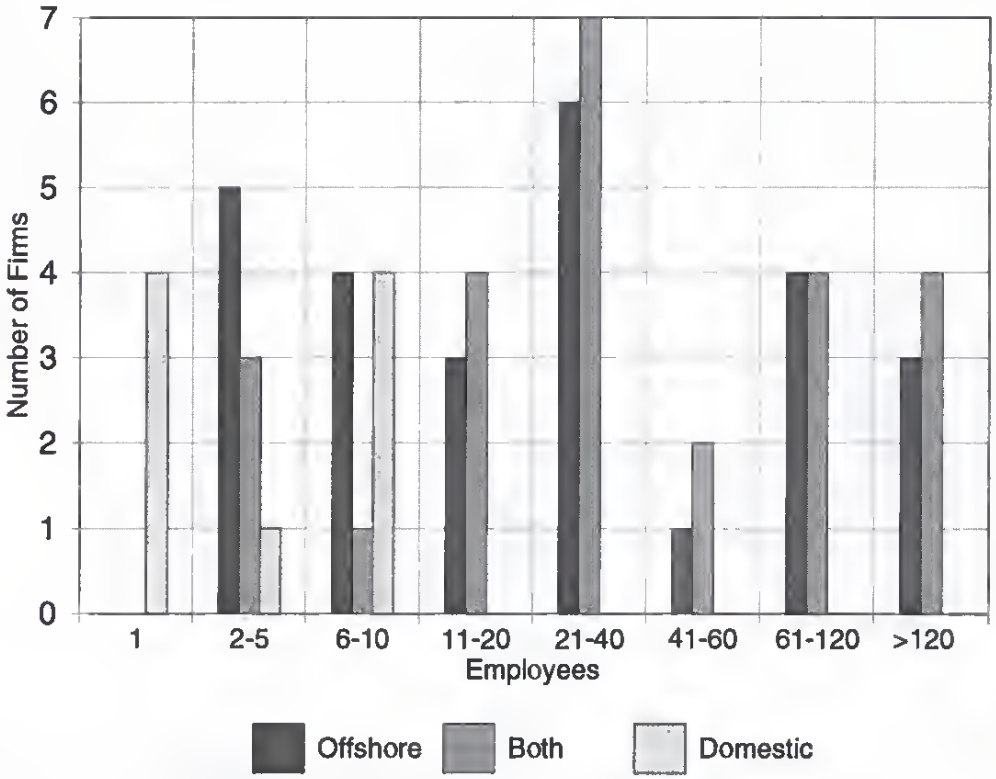

Figure 4.7. Firm size by type of service offered.

Local-Global Linkages

Figure 4.8 and Table 4.6 show how the "local" (the Isle of Man) links into the "global" (the rest of the world). Survey respondents were asked with which parts of the world their offices were in contact on a daily or very regular basis. Distinct patterns emerged, with an evident distance-decay effect illustrated by the large number of linkages

with the U.K., Ireland, and other E.U. countries. Large numbers of linkages also take place with North America, other offshore financial centers throughout the world, South Africa, and the Middle East. These linkages comprise every type of business communication--be it with clients, financial markets, or other offices within the specific corporate organization. Many of the linkages to other OFCs are with other offices in the same corporate organization, illustrating the trend of establishment of "offshore groups" within the corporate organization. This appears to be particularly evident within the banking sector.

In addition, firms were asked about their *local* linkages and several interesting patterns emerged. Respondents were asked what kind of local linkages or connections they performed on a daily or very frequent basis. Table 4.7 shows that the types of linkages were classified in three ways: linkages with (1) other professionals, i.e., bankers, accountants, lawyers, (2) government agencies, i.e., regulators, tax office, (3) clients, i.e., HNWI.

The greatest number of local linkages (22) were between the 26 firms providing offshore services and other professionals; it was "other" firms, followed by banks, that established most links. Those 25 firms offering both offshore and domestic services had the second largest number of local links with clients (18) and with other professionals (16). Almost half of the linkages (48%) were within the financial service sector itself to other professionals. This finding tends to refute the earlier allegation of a trend toward "one-stop shopping" for financial services and leans more toward the assertion that *many* firms are involved in the provision of financial services to offshore clients. Synergistic linkages appear particularly strong for the banking and "other" sectors and, within the latter, for law firms, company and trust formation/administration firms, fund management companies.

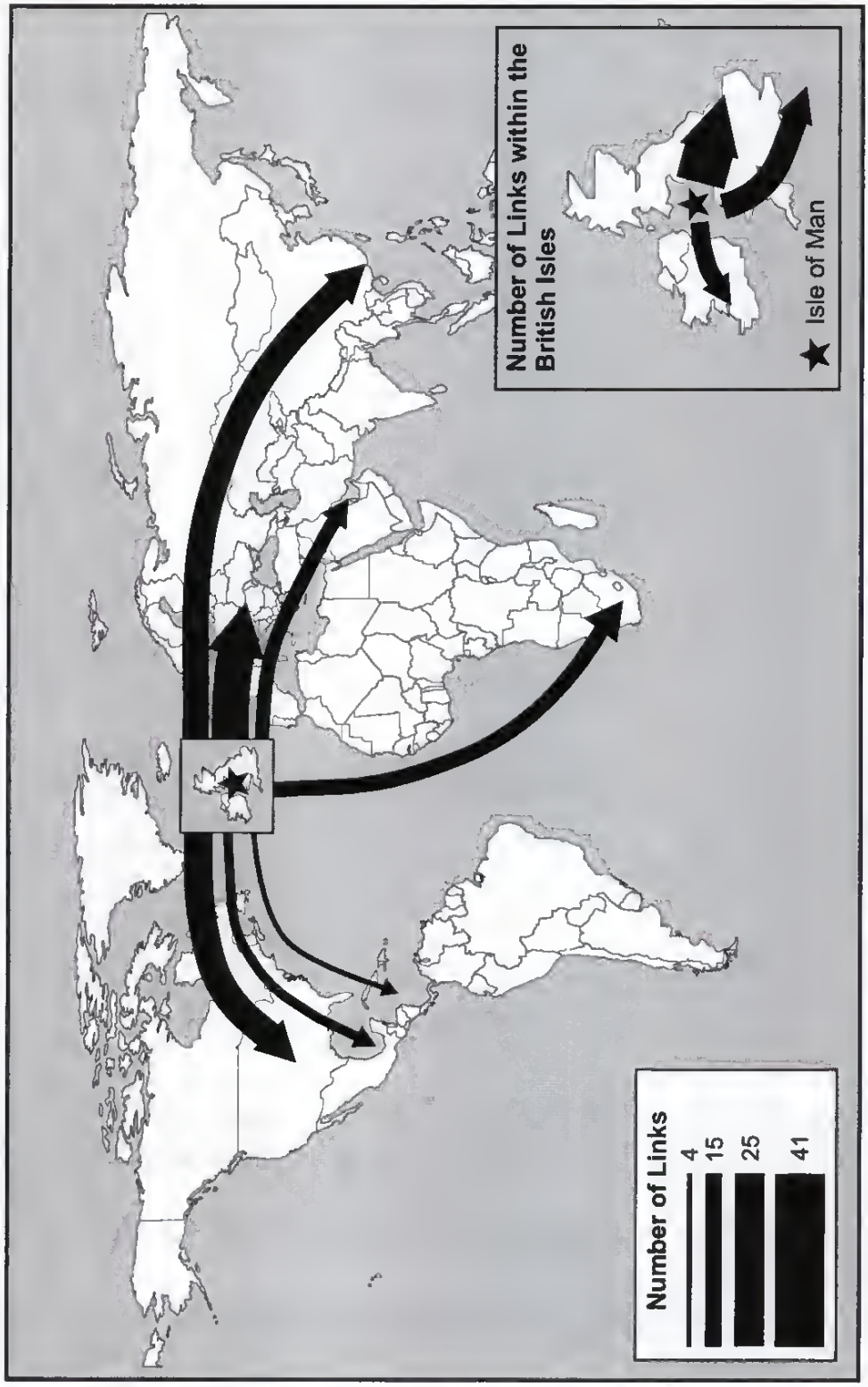

Figure 4.8. Local-global linkages.

Table 4.6. External linkages.

EXTERNAL LINKAGES	# FIRMS	% FIRMS
ONSHORE		
- UK	38	63
- E.U.	24	40
- North America	22	37
- South Africa	12	20
- Middle East	11	18
- Ireland	10	17
- Far East	7	12
- Latin America	6	10
- Eastern Europe	1	2
OTHER OFCS		
- British Isles' OFCs	18	30
- Asian OFCs	18	30
- European OFCs	16	27
- Caribbean OFCs	9	15
TOTAL LINKAGES	192[a]	

Source: author's survey.
Note: [a] total linkages are greater than total number of firms because some firms have several linkages.

Table 4.7 Local linkages.

Type of Service	Professional	Government	Client
Banking	11 (18%)	6 (10%)	9 (15%)
Insurance	8 (13%)	2 (3%)	5 (8%)
Accountancy	8 (13%)	3 (5%)	9 (15%)
Other	15 (25%)	6 (10%)	9 (15%)
Offshore	22 (37%)	6 (10%)	2 (3%)
Domestic	4 (7%)	1 (2%)	9 (15%)
Both	16 (27%)	6 (10%)	18 (30%)
Total linkages	42 (48%)	17 (19%)	29 (33%)

Source: author's survey.
Note: percentages rounded to the nearest whole number.

Frequent linkages with government agencies form less than 20 percent of the total linkages. This is probably due to the fact that interaction with regulators takes place either on a sporadic needs basis, or on the regular quarterly (3 month) basis required by the regulators.

Over one third of the local linkages are with clients which are either individuals or other firms in the island--the latter being particularly important for accountancy firms: even banks have to be audited.

Networks

This section analyzes further linkages in the form of *network* participation. Table 4.8 shows the importance of networks as perceived by survey respondents. Seventy percent of the firms surveyed were either part of an international corporate network, or a U.K. or Irish national network. Those networks include banking, insurance, accountancy, and shipmanagement corporate organizations. The individuals participating in the survey were asked if they belong to any other types of network: over 70 percent belong to a "functional" or professional network, such as the Isle of Man Bankers Association, the Manx Insurance Association, or the Isle of Man Fund Managers Association. Furthermore, almost 50 percent of the respondents belong to a general business/social network with the most cited example being the Isle of Man Chamber of Commerce. In addition, one quarter of the respondents use their own personal business networks, and state that building trust through these networks is a critical element in the way that they do business and a major source of new business.

The results of this data analysis and the fact that so many financial practitioners participate in some form of network warranted further in-depth analysis. Because the findings from this part of the study were drawn from open-ended subjective-type questioning, qualitative analysis was chosen as the method of analysis (see Yeung, 1995). Qualitative analysis has its roots in anthropology, sociology and education and seeks to "resolv[e] data into its constituent components to reveal their characteristic themes and patterns" (Coffey and Atkinson, 1996, p. 9). Although criticized as lacking rigor, validity and reliability,

qualitative analysis is seen by many as "structured, formal, bounded, systematic, grounded, methodological, particular, carefully documented, and impassive" (ibid.). Indeed, within the new field of geography of finance, such analysis appears to be an appropriate method to use when exploring what Leyshon (1997, p. 389) calls "alternative theoretical approaches to money." These approaches draw "inspiration from other intellectual traditions, such as critical social theory, cultural studies, and feminism . . . And emerged out of a general sense of unease and dissatisfaction with prevailing social theory and political economy account . . . [suggesting] that the economic world is too important, and too complex, to be left to economists" (ibid., p. 389).

Table 4.8 Network Membership

TYPE OF NETWORK	# FIRMS	% FIRMS
Corporate[a]	42	70
Functional/professional[b]	43	72
Business/social[c]	29	48
Personal[d]	15	25
TOTAL NUMBER OF FIRMS	60	

Source: Author's survey
Note: for example [a] international bank, [b] association of insurance professionals, [c] chamber of commerce, [d] individual contact networks.

Three types of financial services "actor networks" were identified and linkages to the fourth network--the client network--were analyzed (Figure 4.9). The system of offshore financial services networks proved to be dynamic, both in terms of the networks themselves and the individuals comprising each network. Financial services providers belonged to

different kinds of networks (corporate, professional, and/or social) and had several reasons for participating in those networks.

Many respondents belonging to branches or subsidiaries of large transnational organizations used local professional and public-private "policy-driving" committees or networks as a means of participating in the development of the island's regulatory regime which can be seen as a way of indirectly expanding their client-base. Respondents from smaller firms, not part of a large corporate network, used local networks for several reasons, including information sharing and direct marketing strategies. The "social" nature of finance, acknowledged by Leyshon (1997); Thrift (1994); Leyshon and Thrift (1997) appears to hold true in a small place acting as an OFC. Everyone knows everyone else and ease of access to important people was mentioned by several respondents as an advantage of the island.

Three types of networks (corporate, local, and personal) drive the successful provision of offshore financial services and help create the formation of the fourth--the client network. Most of the offshore practitioners in the island are part of, or connected to, large global corporate networks. The strength (or formality) of the links to the network exhibit a number of different dimensions. For example, banking institutions may be described as being "wholly owned subsidiaries" of a U.K.- based parent company, which in turn may be owned by a multinational holding company, so are part of a truly global network. Some insurance companies are part of a multinational corporate network; others rely on indirect links to the global economy through the use of intermediaries (brokers or independent financial advisors (IFAs)). "Other" offshore financial providers tend to participate in global corporate networks in a less formal or rigid structure, or have no corporate network links.

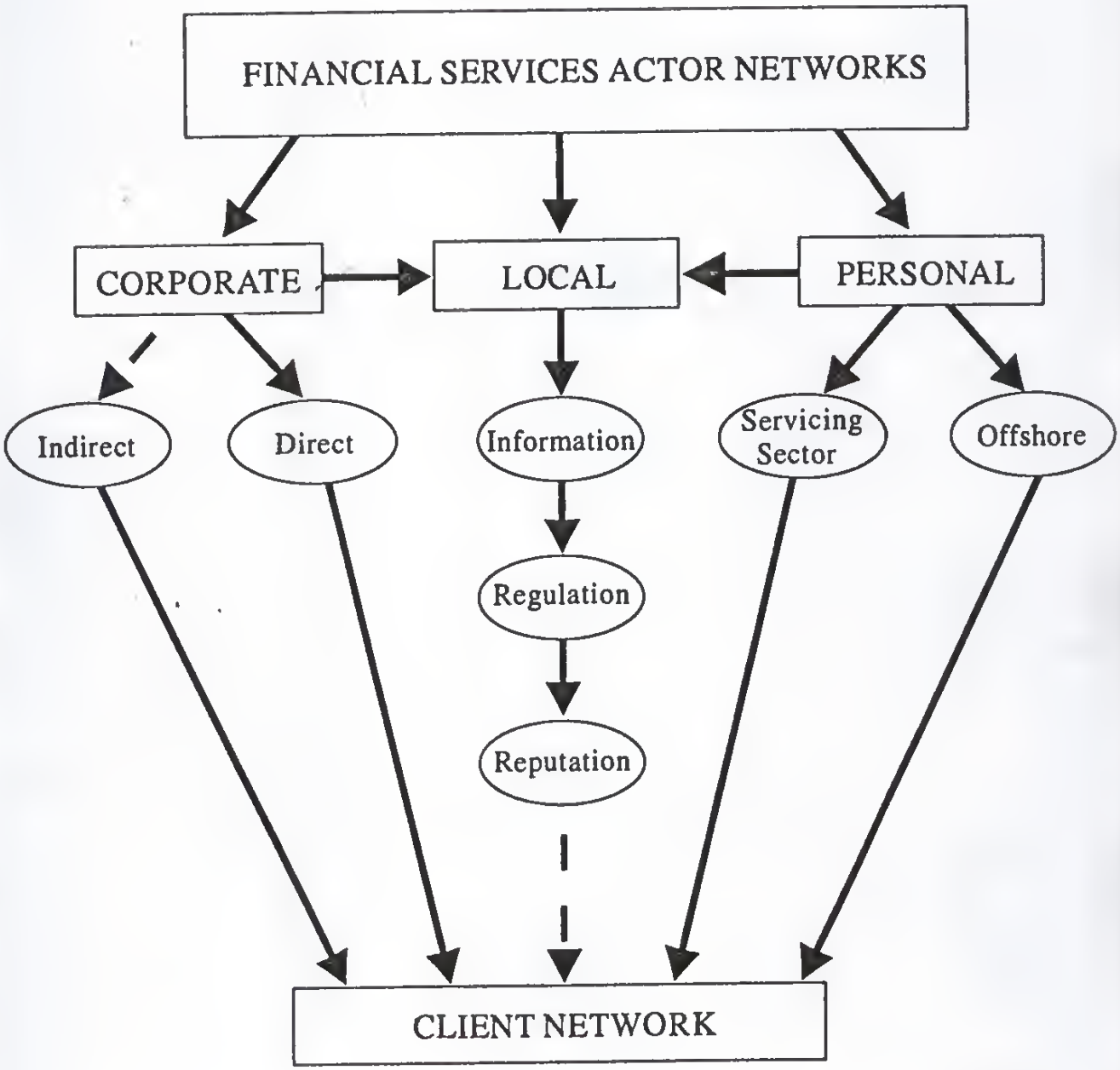

Figure 4.9. Financial services networks.

In general, those firms that are small and privately-owned, with no strong formal links to any corporate network, rely much more on their own personal network of contacts, often established after years in the business. Personal networks play an important role in the establishment and maintenance of a client base for firms outside of the banking or insurance sectors, providing such services as company/trust formation and administration, particularly if the individual respondent traveled widely and lived in a number of onshore and offshore jurisdictions. Furthermore, personal networks play a significant role for individuals whose niche is servicing the Manx financial sector, for example, providing auditing services, legal opinion, or investment advice to other offshore financial services firms in the island. The role played by networks in the growth of the Isle of Man as an OFC is analyzed further in Chapters 5 and 6.

CHAPTER 5
REASONS FOR GROWTH OF THE ISLE OF MAN AS AN OFC

Introduction

Both private sector and public sector respondents were asked why they thought the Isle of Man's offshore financial sector had grown so much over the past ten years. This was an open-ended question with a free-flowing conversation on the part of the respondents and, by its nature, linked in to the other unanswered questions remaining in the survey (see Appendix A for the survey instrument).

Private sector respondents' perceptions regarding the reasons for the growth of the financial sector in the Isle of Man are shown in Table 5.1. Almost half of the survey respondents identified the establishment of a specific regulatory environment in the island as a major reason for the growth of the sector. Almost one-third of the respondents identified "location" as an important factor--this can be interpreted both as physical proximity to service the British Isles' market, and as a time zone factor (Europe rather than the Caribbean or Asia). Specific attributes of the Isle of Man such as lower costs of operation and room to grow were mentioned by almost one-third of those interviewed. This ties into the next most popular reason--the acknowledgment that the Channel Islands are "full up"--leading to an assertion by many survey respondents that, until recently, "it has been growth by default".

However, this somewhat negative portrait drawn by some of the respondents is tempered by the recent initiatives put in place by the Manx Government and by the private sector (for example, the Manx Business Connection) to actively promote and market the island as a safe, confidential and reputable *Wealth Management Centre*. This issue is addressed further in chapter 6.

Table 5.1 Reasons for initial location of firm in the island, and/or growth of business for the firm.

WHY LOCATE IN THE ISLE OF MAN?	# RESPONSES
Specific regulatory environment	26 (43%[1])
Location (service a specific geographic market)	19 (32%)
Lower costs of operation (land, labor, housing)	18 (30%)
Room to grow (land space, availability of labor)	18 (30%)
Channel Islands are "full up"	15 (25%)
Advantageous tax regime	14 (23%)
Professional infrastructure	10 (17%)
Personal reasons/already located in the island	6 (10%)
Individual moved from a previous job in the island	5 (8%)
TOTAL RESPONSES	131

Source: author's survey.
NOTE: [1] figures in parentheses are % of total number of firms giving each response.

This chapter analyzes the respondents' views regarding the growth of the financial services sector by placing their statements within the conceptual framework developed in Chapter 3. First, though, the premise (as discussed in Chapter 3) that the driving force behind the initial establishment of an offshore financial sector was the creation of a *tax haven* in the 1960s will be addressed.

The IOM: A Low Tax Area

As the island's beginning attempts to create an offshore financial services sector were through the passage of legislation establishing itself as a low tax area, it is pertinent to begin by first analyzing survey respondents' perception of the importance of *low taxes* in driving the recent growth of the sector. Table 5.2 shows the responses ranging from "extremely" important to "not" important regarding this issue. Although no one category of importance was dominant, a surprisingly large number of firms (almost 50 percent) thought the low tax issue was of "little", or "no" importance, or wasn't even considered as a major factor (see the N/A category in Table 5.2). Why is this? Low taxes were significant when the island was establishing itself as a "tax haven" in the 1960s, but they are not so important now because all OFCs have low-tax regimes--therefore the tax issue is often taken as "given". More important is the ability to create certain *tax structures* made possible through the existence of specific pieces of financial legislation. Each OFC has a unique legislative and regulatory regime and often the choice of a particular OFC on the part of a client (or more usually, that client's financial advisor) is based upon the type of tax structure required for that client's portfolio. Slightly more than half of the respondents for whom the tax issues was "important" to the growth of their business in the Isle of Man are relative newcomers to the island, having been present in the island for less than 12 years and obviously taking advantage of recent legislative changes to the regulatory regime.

Table 5.2 Importance of low taxes.

IMPORTANCE	# FIRMS	%
extremely important	14	23
quite important	10	17
moderately important	7	11
little importance	13	22
not important	4	7
N/A[a]	12	20
TOTAL	60	100

Source: author's survey.
NOTE: [a] N/A refers to not applicable OR no answer. These firms provide either only domestic services whose growth was not conditioned by low taxes, or did not refer to taxes in the interview.

Because the most common reason for the growth of the sector (Table 5.1) was the existence of a specific regulatory environment, the next section will further explore and analyze the role of regulation.

Role of Regulation

Table 5.3 shows the perceptions of the role and importance of financial legislation and regulation enacted by the Manx parliament (known as Tynwald), to the growth of the respondents' own firm and the financial sector in general. Nearly 60 percent of the respondents felt that the program of financial legislation put in place by Tynwald was either extremely or quite important to the growth of the sector. However, again a surprisingly large number (13 firms or 21 percent) thought that the establishment of financial legislation was of little or no importance to the growth of the sector.

Table 5.3. Importance of financial legislation and regulation.

IMPORTANCE	# FIRMS	%
extremely important	26	43
quite important	9	15
moderately important	6	10
little importance	9	15
not important	4	7
N/A[a]	6	10
TOTAL	60	100

Source: author's survey
NOTE: [a] N/A refers to not applicable. These firms provide only domestic services whose growth was not conditioned by legislative action in any way.

Analysis of importance of financial legislation by major financial service provided is seen in Table 5.4, which shows that "extremely" is the most frequent response for all sectors. Out of a total of 15 banking sector respondents, 13 thought that the financial legislative and regulatory regime was either extremely or quite important in explaining the growth of the sector as did 9 (out of 14) insurance firms and 8 (out of 19) "other" firms. One bank, 2 insurance companies, 4 accounting firms and 6 other firms saw the legislative and regulatory program having little or no importance in explaining the growth of their firms.

Table 5.4. Importance of financial legislation by financial service sector.

IMPORTANCE	# BANK	# INS	# ACCT	# OTHER
extremely important	8	6	5	7
quite important	5	3	-	1
moderately important	1	-	2	3
little importance	1	1	2	5
not important	-	1	2	1
N/A	-	3	1	2
TOTAL	15	14	12	19

Source: author's survey.

Further insight into the importance of regulation and the major firm characteristics used to document the growth in the sector (see Chapter 4) was explored through construction of a multiple regression model of the following form:

$$Y = \beta_0 + \beta_1 X1 + \beta_2 X2 + \beta_3 D + \epsilon$$

where Y = importance of regulation (using Likert scale where extremely important = 5 and not important = 1)

X1 = years firm has been doing business in the island

X2 = number of employees

D = dummy variable where 1 = firm is part of corporate network and 0 = firm is independent.

This model produced an adjusted R square of 0.27 and a significant F at the 0.05 level (see Table 5.5 for full regression results). The independent variables X1 (years) and D (corporate structure) are significant at the 0.05 level: In other words, the length of time the

firms have been present in the island and corporate ownership structure are related to perceived importance of regulation. However, rather than further refine a statistical model to prove the importance of the role of regulation, this research project adopted qualitative analysis to explore the richness of the survey data.

Table 5.5 Regression results.

Regression	Statistics		
Multiple R	0.55572		
R Square	0.308825		
Adj. R Sq	0.267354		
Stand. Err	1.180189		
Obs	54		
Anova	df	F	Signif F
Regression	3	7.446858	0.000324
Residual	50		
Total	53		
	coefficient	t stat.	P value
Intercept	3.038558	8.987857	3.06E-12
X1	-0.01337	-2.86988	0.005887
X2	0.003491	1.703662	0.094302
D	1.204506	3.225036	0.002159

Source: author's survey.

The Importance of Financial Legislation and Regulation

Comments regarding the importance of financial legislation and regulation were varied in nature and scope. Many respondents stated that the government program of legislative changes after the collapse of the Savings and Investment Bank in 1982, developing a more rigorous regulatory regime, was crucial to re-establish a positive reputation and confidence in the island. The fact that the island has had a depositors protection scheme for banking services since 1991 and is the only OFC to have one is seen as a significant comparative advantage. One respondent noted that it is successful *supervision* rather than regulation per se which is important in underpinning the island's reputation.

Private sector respondents' perceptions of the role of the Manx Government in stimulating the growth of the offshore financial sector by establishing the regulatory regime were varied. Some thought that the government (particularly the Treasury Department) had the correct attitude toward growth and were approachable, responsive, and willing to listen to the private sector. Others were critical of "part-time politicians" who would not listen and did not understand some of the intricacies of offshore finance. Some thought that the legislative procedure used by the Manx Government is reactive, slow, and cumbersome, whereas others thought the government was quick to react to the needs of the private sector. One respondent acknowledged that "legislation is the foundation of the product you sell, but the IOM is slow to change and the elected government is too reliant on civil servants and the Financial Supervision Commission (FSC)". However, a large number of respondents cited

the creation of the FSC in 1983 as the critical turning point for the island's attractiveness to legitimate offshore investors.

One of the common themes that emerged through qualitative analysis of the data was identification of very distinct feelings regarding the relationship between private sector respondents and regulators[1]. Many respondents talked about the need for a *balance* between under-regulation and over-regulation and the difficulty of creating and sustaining that balance. One private sector respondent talked about the existence of (and need for) "healthy tension" between the private sector and regulators. Some respondents felt that the FSC had "got it right" and are approachable, pragmatic, willing to listen, user friendly, and have fostered a relationship of mutual trust and understanding with the private sector. Others thought that, when first established, the FSC did exactly the right thing but now the regulatory body is too reactive (rather than proactive), bureaucratic, inflexible, and onerous to deal with. Another respondent posed the rhetorical question: "who regulates the FSC?"

Some respondents were critical of the way in which the FSC has followed the style of financial regulation found in the United Kingdom, whereas others saw this to be a positive feature. One respondent said that the island has "developed a supervisory regime which is not onerous, but is firm. The rules and regulations are simple, straightforward, and easy to administer when compared to the U.K."

Another theme to emerge from qualitative analysis was the perception that size of firm may influence the attitude of regulators in their supervisory role--some smaller firms

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[1]Differences of opinions within the private sector regarding the regulatory bodies could be broken down by sector; however confidentiality bars further discussion and analysis at this level of detail.

thought that the FSC "picked on the small guys" and were more cooperative with the larger firms. A large-firm respondent even thought that they might have had more "hassle" if they were smaller. Overall, consensus regarding the need for a body such as the FSC for outsider confidence was apparent.

Different perceptions regarding the *role* of regulatory bodies emerged from qualitative analysis. Some respondents thought that the FSC should have a marketing role as well as a regulatory and supervisory one. In many instances, this led to a comparison between the FSC and the other major regulatory body in the island--the Insurance Authority, established in 1986. Many more positive impressions were given about the Insurance Authority. It is seen as flexible, friendly, pragmatic, proactive, less costly, and much more market conscious than the FSC. The Insurance Authority is seen to have a stronger (or at least, more overt) marketing role for "IOMplc" than does the FSC. Public-private interaction with respect to marketing the island as an OFC is further analyzed in chapter 6.

The findings regarding the importance of financial legislation and regulation lead on to consideration of two important facets of regulation. First, who has to be regulated, and by whom? Furthermore, which firms have to be regulated by a Manx regulatory body and which do not? Second, how have legislative and regulatory changes outside the Isle of Man affected business practices in the island?

Who is regulated?

All providers of financial services will argue that self-regulation is a constant presence in business practice through the functioning of the market--what differs is the *mechanism* by which regulation and, more importantly, supervision take place. All banking

institutions, financial businesses, and collective investment schemes in the Isle of Man are licensed and supervised by the Financial Supervision Commission (FSC); likewise, all insurance businesses are authorized by the Insurance Authority.

Other firms offering financial services, often in the form of financial advice or tax planning or company/trust formation, are not regulated directly by the two Statutory Bodies above. However, they are classified by the FSC as "Recognised Persons" and, as such, are exempt from the requirement to hold an investment business license because their investment business is regulated by an alternative "Recognised Regulator" (Isle of Man Financial Supervision Commission, 1995). Recognised Regulators are, with the exception of the Isle of Man Law Society, located outside the island: for example, The Institute of Chartered Accountants in England and Wales, and the Securities and Futures Authority Limited. Furthermore, some of these service providers stress the importance of market regulation in addition to their professional regulation: if they were not providing an exemplary service, they would go out of business.

Onshore regulation

It is crucial to consider legislative changes in the Isle of Man in the light of new legislation in the U.K.--the nearest "onshore" place as legislative changes onshore can drive growth offshore. For example, growth in business volume for some building societies in the island was driven by recent changes in legislation in the U.K. which introduced separate tax allowances for married women.

In general, the relationship between U.K. legislation and Manx legislation for some building societies in the island may be seen as a process by which the former (U.K.)

established "enabling" legislation and the latter (Isle of Man) "sympathetic" legislation. In other words, after being given the chance to exploit a market because of changes in onshore legislation, offshore legislative changes were put in place to ensure the appropriate legislative framework to take full advantage of the "new" market. This proves beneficial both for the specific financial firms involved, and for the island in its quest for continued growth and development.

The other side of this close relationship and interaction with the "onshore" jurisdiction, however, is a negative one, and can be best characterized as a position of vulnerability of the island to other legislative changes in the U.K., which may constrict the island's offshore business rather than expand it (as in the case of the example above). The overwhelming majority won by the Labour Party in the 1997 general election, after 17 years of Conservative rule, raised concerns throughout the British Isles' offshore centers. The vulnerability of the British Isles' OFCs has been noted previously (Hampton, 1996a) and, due to their constitutional relationship with the U.K. as Crown Dependencies, they are placed in the position of having to wait to react to the direction of offshore policy implemented by the new administration in the U.K. (Ramsay, 1996).

The Role of Networks in Creating the Regulatory Regime

Financial services is a segment of the global economy where the creation and maintenance of *trust* is a vital part of the successful functioning of the system. The reputation of an OFC is based upon the creation of a spatially focused regulatory and supervisory regime with the aim of concurrently exploiting *and* legitimizing regulatory

differences to offer advantages to global investors which cannot be found elsewhere. In the Isle of Man, the creation of such a regime has occurred through the successful functioning of local networks and the existence of what Amin and Thrift call "institutional thickness." Because of local interaction through inter-firm *and* public-private networking (the *local* network, see Chapter 4, Figure 4.9), issues are identified that are critical to the attractiveness of one OFC as compared to others. The willingness of both public and private sectors to work *with* each other in the creation of regulatory-based legislation and the subsequent agreement of the private sector to be monitored *by* the public sector seem to be essential in the establishment of a superior reputation.

Many of the functional networks identified in Chapter 4 send representatives to the public-private "policy-driving" consultative committee networks established by the Isle of Man Government Treasury Department. "In order to assist it with the carrying out of its various duties, the [Manx] Treasury has four ongoing Consultative Committees which include members drawn from the private sector" (Solly, 1995). According to the Treasury Minister, this interactive relationship between the public and private sector is unique among OFCs.

The four Committees meet on a regular quarterly basis with both the private and the public representatives having the ability to introduce items onto the agenda. The four Consultative Committees represent different segments of the financial sector and are as follows:

(1) the Banking Consultative Committee

(2) the Insurance Consultative Committee

(3) the Finance Committee of the Chamber of Commerce Consultative Committee

(4) the Professional Consultative Committee.

Figure 5.1 illustrates the "tree-like" structure of this public-private process with specific reference to the banking sector. Individuals from the different banking committees or associations are elected to represent the interests of their committees at the quarterly meetings of the Banking Consultative Committee. It is through this systematic dialogue, free-flowing discussion, and interaction that many of the new pieces of financial legislation are born.

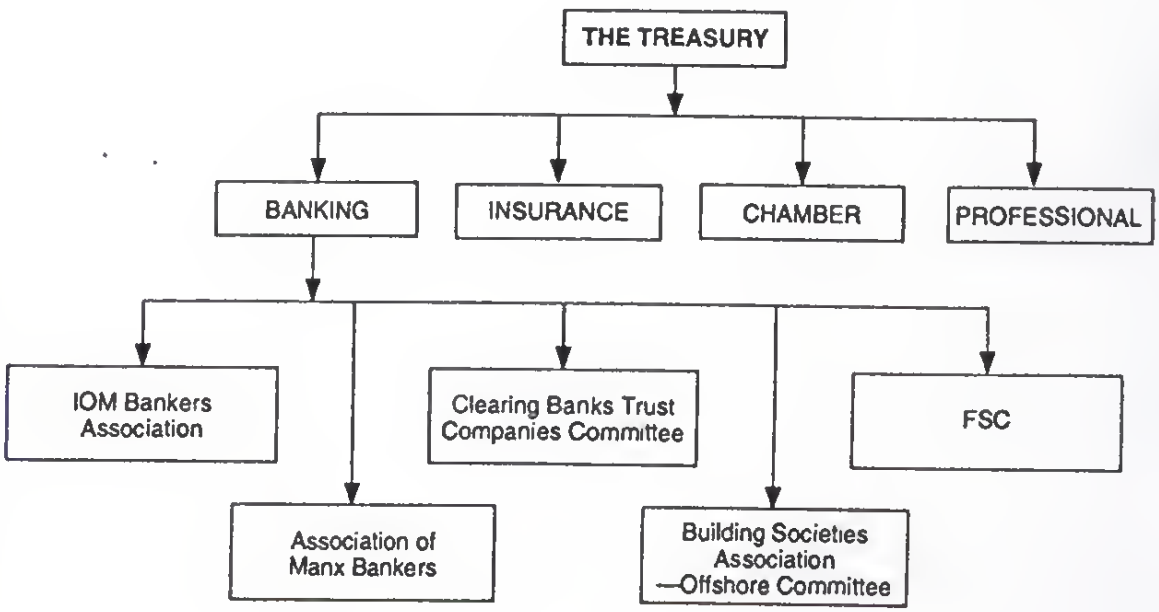

Figure 5.1 Public-private interaction in the financial sector.
Source: adapted from Solly (1995).

Those actors from large multinational firms who have the benefit of their own corporate networks (and in some instances do not even provide services to local residents) participate in local networks in order to help craft the regulatory regime. Actors representing the "big" players tend to have a high community profile and are active in many local networks. They have the ability to diffuse information to the local community and use their own corporate-derived knowledge when participating in the policy-driven Treasury consultative committees.

The following statements illustrate some of the attitudes towards local networks, when asked why respondents participate in such networks. Some saw local networks as a means to share (or gain) information *and* as a means to influence the government with respect to further development of the financial regulatory regime. Confidentiality requirements dictate that respondents cannot be identified by sector (for example, banking, insurance, accountancy) but all sectors are included in the following respondent statements about the nature and purpose of networks.

(1) Information and influence

> "[A] forum to discuss issues of interest to all of us, to air problems, and to find solutions between us. It's a means to 'flag' issues. It's a 2-way process [and I] never have the feeling that we have meetings for the sake of having meetings. The beauty of a small place is that you can pop-in; the government encourages face-to-face interaction" (respondent #31).
>
> "[A] way of sharing information, 2-way communication, influencing" (respondent #2).
>
> "[To] keep up-to-date and meet with people. The advantage of the I.O.M. is ease of access to important people" (respondent #12).
>
> "To get to know people and businesses in I.O.M., and people who make decisions. The I.O.M. is very social" (respondent #58).

Second, there were those who mentioned only the ability to influence the government:

(2) Influence

"Useful to structure [the] regulatory environment" (respondent #3).

"Useful to represent the I.O.M. or act as a lobbying front" (respondent #20).

"Valuable for a unified push either for or against legislation" (respondent #21).

"Channel to be able to make representations to the government. Government is approachable" (respondent #50).

Many private sector respondents saw local networking as a valuable tool to use to interact with the public sector, inform government officials of their needs, and help design legislation to further refine the regulatory regime.

The Labor Issue

The rapid growth of the island's offshore financial sector over the past 10 years created some problems, particularly with respect to the supply of labor. Two main issues of concern addressed by respondents were *quantity* of labor and *quality* of labor. Table 5.6 shows unemployment rates for the island during the 1990s.

Table 5.6 shows that the unemployment rates were very low in the late 1980s and in 1990. The tight labor market at this time was attributed by many respondents to the arrival of the labor-intensive offshore life insurance companies beginning in the late 1980s. Some respondents accused this sector of "poaching" employees that had been previously trained in other sectors, by offering higher wages and benefits. Many respondents complained about

the cost of labor in the late 1990s, often citing the fact that secretarial staff were being paid City of London salaries because of increased demand for semi-skilled labor and lack of supply. Some also were critical of the labor force itself for being fickle, mobile, and wanting to move within the island from sector to sector for small salary increases. In this sense, the "smallness" of the island was viewed in a negative way.

Table 5.6. Unemployment 1987-1996.

YEAR	# UNEMPLOYED (%)
1987	1550[a]
1988	900[a]
1989	533[a]
1990	592 (1.8%)
1991	1,112 (3.4%)
1992	1,527 (4.6%)
1993	1,654 (4.9%)
1994	1,685 (5.0%)
1995	1,513 (4.5%)
1996	1,211 (3.5%)

Source: Isle of Man Government, 1993,1996.
Note: [a] estimate calculated by author from Government figures.

The major reason for labor supply problems is the existence of a form of immigration control whereby all workers, unless Manx-born or married to a Manx, are required to obtain a work-permit from the Manx Government in order to gain employment in the island. The issue of work-permits was frequently mentioned by private sector respondents, most of whom had positive dealings with the government with respect to *highly skilled labor*. In this

case, most respondents argued that it was difficult to recruit "quality" labor in the island and work-permits for highly skilled labor from "outside" were usually easy to obtain. Respondents acknowledged that most top management levels are non-Manx, but some mentioned that it was sometimes difficult to recruit labor from the outside to come to live and work in the Isle of Man--"City" salaries may not compensate for the lack of cosmopolitan city life! Some respondents noted that work-permits for semi-skilled staff can be very difficult to obtain and accused the government of being too rigid, bureaucratic, and stifling growth in the island.

Both *cost* and *availability* (through issuance of work-permits) of labor in the Isle of Man were seen by some respondents as positive factors when compared with other offshore jurisdictions. For example, the Channel Islands, Bermuda, and Switzerland were seen to be both costly and *exclusive* when considering labor issues and the Isle of Man is seen as a cheaper and less labor-restrictive jurisdiction with (literally) room to grow. When labor cannot be recruited locally, many firms in the island look to Ireland (particularly Dublin) as a source of good, well educated labor to import. Critically, for the Isle of Man, some respondents even stated that Dublin's International Financial Services Centre (its "offshore" center) is considered to be a viable jurisdiction for further expansion--in other words corporate expansion would take place off-island to benefit from Dublin's competitive advantage of cheaper skilled and semi-skilled local labor with, what one respondent said, "a much better and more cosmopolitan attitude to offshore finance".

Manx Government efforts to encourage and promote financial sector skills and training in both high schools and the (only) college of higher education in the island were

noted and appreciated by some private sector respondents. The issues of "Manx" versus "non-Manx" workers was brought up by a number of respondents: some lamented the insular--almost closed-minded--attitude of the locals; others were proud of the fact that they wanted (and had) a "local" workforce. One respondent said that "we have a policy of recruiting a Manx workforce. The Manx know how things work around here." Another said that "we don't want Manx who have never been off the island, we want those (Manx) who have been away for a while." Another noted the existence of a "brain drain" whereby most good Manx students leave to go to university in Britain and never come back. However, this view was challenged by someone else who said that increasingly Manx students *are* coming back after university, particularly to work in the accountancy and law professions.

This final observation leads to consideration of differences in career path trajectories between different sectors. Traditionally, the banking sector in the UK (and *de facto* Isle of Man) has had a rigid intra-corporate career path (cf Beaverstock, 1994) involving many moves up the corporate ladder. The vast majority of extreme upper management positions in banks in the Isle of Man are held by mobile non-Manx who might be expected to stay in the island for 5 to 7 years before being promoted and relocated elsewhere. Other sectors do not appear to follow this rigidity of structure. For example, the accountancy sector now requires a University education for its skilled workers and given that there is no such institution in the island, such firms recruit both returning Manx graduates and British and Irish nationals wishing to undergo their accountancy training in the Isle of Man. Furthermore, in some instances, already qualified professionals in other sectors deliberately choose to move to the island for quality of life issues: the Isle of Man is seen by some as a safe, relatively slow-paced environment and a good place to bring up children.

Another solution to labor supply problems in the island proffered by some respondents was notion that information technology (IT) would replace the need for "warm bodies". A few respondents acknowledged that the development of IT systems to replace labor was a deliberate corporate strategy and were very satisfied with the technological and communications infrastructure available in the island. The role of communications technology is addressed in the next section.

The Communications Infrastructure

Survey respondents were asked how they rated the communications infrastructure in the island with respect to both telecommunications and physical communication links to and from the island. The island's sole telecommunications provider--Manx Telecom[2]--is highly regarded by most private sector respondents. The infrastructure is perceived to be up-to-date, "first-class", more sophisticated than that in the U.K., and seen by some to have developed in a way to meet the needs of the financial sector, particularly with respect to information technologies and mobile phone systems. Importantly, sophisticated IT, combined with relatively low labor costs, is seen by some as the major driving force behind the island's growing development as a *back-office* for offshore financial services for transnational banks and insurance companies. One respondent pointed out that because the Isle of Man is a "late-starter" when compared to the Channel Islands, it has more flexibility with the

[2]Manx Telecom (MT) is a fully owned subsidiary of British Telecom, created in 1987, and operating with a 20 year licence awarded by the Manx Government which requires that 15% of annual profit be paid to the government. MT has invested over £25 million in developing the island's telecommunications infrastructure and has seen subsequent growth in international calls of over 20% per annum.

implementation of new communications technology, greater capacity for change, and is actually now more sophisticated in its telecommunications infrastructure than either Jersey or Guemsey. New technologies are often introduced in the island as an experiment or pilot study *before* being adopted in the U.K. The major concern of respondents had to do with cost--Manx Telecom is a monopoly and some believe because of this they charge too much.

In general, *physical* communications and accessibility--particularly with reference to airline connections with London--were a much greater item of concern for many respondents. The major problem was cost, but frequency of service was another concern. Some respondents stressed the superiority of airline services and connectivity in other British Isles' offshore centers and perceived the Isle of Man having a distinct disadvantage, particularly with the lack of direct flights to financial centers in Europe. A few respondents felt that the existence of a frequent daily airline service to London was sufficient for their needs and saw London as the convenient meeting place for all those engaged in provision of offshore financial services in the British Isles' OFCs. The importance of London, the U.K., and the rest of the British Isles is addressed in the next section, which analyses political factors and their influence in the growth of the Manx financial sector.

Geopolitics of Offshore Finance

The importance of the relative location of the Isle of Man and its political relationship with the United Kingdom and the European Union were perceived in many different ways by survey respondents. According to one survey respondent:

> the political relationship with the U.K. is important as it is important to be seen to be independent but it is good to have an affiliation with the U.K. and an indirect link with the European Union.

The political stability afforded by such connections are seen by many to be critical when considering more volatile offshore jurisdictions outside the British Isles.

Many survey respondents thought that the *similarities* between the island and the U.K. in terms of political and judicial regimes (both are based on English Common Law whereas Civil Law forms the foundation of the Channel Islands' judicial system) acted in a positive way in terms of client confidence and trust in the way in which the island's offshore financial instruments were constructed. According to some respondents, of particular importance as a factor of comparative advantage for the island is the very English notion and concomitant legal structure of "Trust" which is not legally recognized in many other OFCs.

The perception of being offshore but "very British"--and therefore secure and stable--apparently creates a sense of well being and confidence in the island on the part of clients. The astute observation that the Isle of Man takes more of a lead from the U.K. than do the Channel Islands because the island is "newer at the game" was made by one respondent. Furthermore, accessibility to and from the island and connectivity to both Ireland and the U.K. were seen as important attributes of the Isle of Man, particularly when compared to the Channel Islands, whose links are stronger with London and the south of England.

The close political and economic ties existing between the island and the U.K. were also seen in a negative light, particularly from the firms' perspectives. The island has a "Common Purse" agreement with the U.K. whereby the island "agreed to keep all Customs

and Excise revenues at the same rates and subject to the same conditions and reliefs as in the United Kingdom" (Solly, 1995). Such revenues include the value added tax (VAT) which has to be added to certain financial services. This puts the island at a disadvantage when compared to the Channel Islands, which do not have such an agreement and do not impose VAT on financial services. In addition, perception as being very close to the U.K. raises concerns by British nationals or expatriates regarding beneficial ownership and heirship issues.

The Isle of Man's and the Channel Islands' relationship with the European Union was established by Protocol 3 of the Act of Accession of the U.K. to the E.U. in 1973, which established a "loose" relationship with the E.U. whereby common customs duties and charges were imposed but island residents cannot benefit from provisions relating to free movement of persons and services within the Union. Again, this was perceived by survey respondents in both positive and negative ways. Concern that the E.U. may become more invasive with respect to the workings of offshore finance was expressed by some. However, some saw that linkages to the E.U. meant that trade (in financial services) could take place with E.U. jurisdictions. In addition, being within the VAT umbrella permits the island to be within the main tax umbrella of Europe--something that the Channel Islands do not have.

Comparative disadvantages exist between the island and Dublin with respect to some offshore financial structures. For example, the Isle of Man is not a good jurisdiction for mutual funds because they cannot be marketed directly to the E.U., whereas in Dublin they can because Ireland is a full member of the E.U.

Relative location of the Isle of Man varied in importance by financial sector. Some offshore financial services are provided through the use of intermediaries--brokers and independent financial advisors (IFAs)--resulting in original onshore client and Isle of Man offshore service provider never meeting each other. In this case, clients' perception of the Isle of Man, right down to its location, does not matter. The brokers and IFAs are, in essence, the clients of the Manx offshore sector and it is they who have to be "courted" and impressed with the financial instruments and tax structures able to be created in the island. Other forms of offshore financial services and instruments necessitate personal visits to the island, and it is then that the island's reputation as, in the words of one survey respondent, the "most northerly, windiest, and wettest OFC in the world" come in to play. Some respondents described the island as "tatty" and much less sophisticated than, for example, the Channel Islands. On the other hand, some saw the location of the island as being convenient for clients in Ireland or the northern part of Britain.

Summary

The creation of the Isle of Man's regulatory regime was seen by many private sector respondents as the building block supporting the continued growth in importance of the offshore financial services sector. But it was this factor in conjunction with several other advantages the island has, combined with *disadvantages* apparent in other OFCs, that created sustainable growth. "Growth by default" was the harsh but pragmatic conclusion given by many of those interviewed, because the Channel Islands are expensive and "full-up", Dublin's IFSC has only a limited lifetime to provide offshore financial services, Bermuda has labor problems and is too far away, and Gibraltar and Cyprus have bad reputations.

One of the major private sector criticisms of the Isle of Man Government and the quasi-governmental regulatory bodies is the lack of a concerted effort to market "IOMplc". Most private sector respondents see themselves as being the only salespeople of the island and its regulatory structure and niche advantages. Chapter 6 therefore analyzes recent public-private dialogue addressing the issue of marketing IOMplc.

CHAPTER 6
MARKETING "IOMPLC"

Introduction

The issue of marketing "Isle of Man plc" (IOMplc) is seen by members of the public and private sectors as absolutely necessary for the continued growth of the offshore financial sector in the Isle of Man. Several private *and* public sector respondents acknowledged that the island's initial development and growth as an OFC was "almost by accident". The island's rocky road to maturity as an OFC beginning in the early 1980s (see Chapter 3) saw recognition by politicians and financial practitioners alike that the island's *reputation* as a stable, secure and reputable place to do business was the key to continued growth. As argued previously, in an economic environment where trust, personal contacts, and personal recommendations play such an important role, the issue of reputation of a financial service center is of vital importance. The recent proliferation of OFCs in the global economy results in increasing competition between each place for offshore capital and this competition means that the development of a "superior" reputation becomes a critical marketing tool for OFCs.

In the Isle of Man, the cornerstone of a superior reputation lies with the regulatory and supervisory regime developed through regular interaction and dialogue between politicians, civil servants, and practitioners. The major dilemma (identified as such by both public and private survey respondents) facing those crafting financial legislation is one of

finding an appropriate *balance* between too much and not enough regulation (see also *The Economist*, 1997b).

Within Europe, regulatory balance appears to be as difficult a task for older OFCs as it is for newer ones. Jersey, an older, well-established, and--until recently-- reputable OFC is facing accusations of lax regulatory structures (Sesit, 1996). Luxembourg, another well-established OFC, is facing external regulatory problems as the E.U. tries to "level the playing field" for financial services (Du Bois, 1996).

In the Isle of Man, most private sector survey respondents were happy with the regulatory and supervisory regime now in the place in the island. However, one area of concern reported by several respondents was the lack of a *cohesive* marketing strategy for "Isle of Man plc". After analysis and discussion of survey results identifying niche services and perceptions of major jurisdictional competition, the rest of this chapter addresses the development of both covert and overt strategies for marketing IOMplc.

Niche Services

Survey respondents were asked if their firms provided what they saw as being niche services. Table 6.1 shows the niches can be grouped into two types: functional (particular financial product or service) and geographic (location of clients).

Although the sample is not large, the diversification of the island's financial sector is illustrated by the number of *different* niche products or geographical markets served. A wide range of financial services and products is offered by firms located in the island with some products or instruments being unique. Some of the smaller financial firms in the island

see their service to the offshore sector as being their niche, particularly so in the accountancy field. The island's relative location and political status as a Crown Dependency is reflected by *geographically close links* (i.e., to the UK and Ireland) being the most numerous sources of clients. The global nature of the sector is apparent, though, by the number of expatriate British and Irish nationals served by firms in the island: these clients could live anywhere, although common source areas are the Middle and Far East. A growing niche area served by firms in the island is the "International Offshore" group which is defined as nationals living outside of their home jurisdiction, including for example, American citizens living in London, or South African nationals living in Europe.

Public sector commentary on the island's niche services obviously took a more general perspective and identified the island as being a leader in captive insurance, back-office insurance and banking services, shipping services, and in the creation of particular tax or financial structures that cannot be found elsewhere. Importantly, this expertise or excellence is seen to be *driven by* the existing regulatory regime put in place to legitimize these services, both within the island and to the rest of the world.

Table 6.1. Niche services.

NICHE	# FIRMS
FUNCTIONAL	
- specific service[a]	16
- financial product[b]	11
- asset management for HNWI	8
- domestic financial sector[c]	5
GEOGRAPHIC	
- UK expatriate	8
- International offshore[d]	7
- UK offshore	3
- Irish expatriate	3
- Other expatriate	3
TOTAL	64[e]

Source: author's survey.

Note:[a] e.g. - tax planning, insurance, shipmanagement

[b] specific instrument, e.g. - bond, mutual fund

[c] e.g. - audit, advice/consultancy

[d] non-resident of Isle of Man

[e] total does not 60 because some firms identified more than 1 niche and some firms did not see themselves as providing niche services.

Jurisdictional Competition

Although some financial products or instruments may be unique to the Isle of Man, many services offered in the island can just as easily be provided in any one of tens of other OFCs scattered around the world. Survey respondents were asked who they saw as being their major jurisdictional competition (see Table 6.2).

Table 6.2 Major jurisdictional competition

JURISDICTION	# FIRMS	% FIRMS
Channel Islands	35	58
Dublin (IFSC)	20	33
Luxembourg	7	12
Other European	2	3
Cayman	4	7
Bermuda	4	7
Other Caribbean	6	10
Asian	1	2
Any low tax area	2	3
TOTAL	81[a]	

Source: Author's survey
NOTE: [a] total jurisdictional competition is greater than total firms because some firms see more than one jurisdiction as competition.

Table 6.2 shows that a strong distance-decay effect is in place, with the closest OFCs (Channel Islands and Dublin's IFSC) being identified as major competitors. The Channel Islands are perceived to be the major competition by 58% of the firms in the Isle of Man, followed by Dublin (33%). Moreover it was evident that OFC competition varies by function: Jersey for banking; Guernsey for captive insurance; Dublin and Luxembourg for fund management services which can be marketed directly to the rest of the E.U.[1] Functional expertise relates directly to the evolution of these competing OFCs. Jersey was established

[2]The Isle of Man and the Channel Islands cannot market funds directly to the E.U. because of their unique relationship to the E.U. as set out in Protocol 3 of the Act of Accession of the UK (1973), see Chapter 3 for further details.

as an OFC for HNWI in the 1950s with international private banking as its niche (Hampton, 1996b); Guernsey developed a niche in captive insurance (Stuart, 1996); both Luxembourg and Dublin (IFSC) have deliberately promoted fund management as their niche, the former several years before the latter (Lapper and Stuart, 1996). Furthermore, some survey respondents identified a distinct "pecking order" amongst European OFCs: some perceived the Channel Islands ("older" OFCs) as "snooty", and Malta, Cyprus and Gibraltar ("younger" OFCs) as "unstable with bad regulation".

Interestingly, many survey respondents' perceptions of major competition (i.e., the other British Isles' OFCs) is in direct contrast to most of the corporate offshore banking strategy now in place in the island. Most large banks providing offshore financial services in the island have been reorganized into part of an *offshore group within* the banks corporate structure resulting in places such as the Isle of Man, Channel Islands, and Dublin now working as a team rather than directly competing against each other. Spatial divisions of labor have resulted in the Isle of Man's low costs of operation, space, and room to grow (Table 5.1) driving an increase in *back-office* operations in the island rather than in the more expensive Channel Islands.

Networks as a Marketing Tool

As illustrated in Chapters 4 and 5, the Manx financial services sector is highly networked, profiting from the parochial nature of a small island where just about everyone knows everyone else. Networks are used as both overt and covert marketing tools. As an implicit marketing tool, local networks are used to craft legislation with the aim of massaging

the regulatory regime to enable innovative and unique financial instruments and services to be offered in the island as discussed in Chapter 5.

Participation in local networks was also perceived by some survey respondents as a means to gain information about the financial service sector and possibly new clients, i.e., there were some who recognized the networks as an overt marketing tool as indicated by the statements below:

> "Any local networking is seen as service to the community, and to get better known in the community" (respondent #11)
>
> "Contacts, networking with defined targets. Many of our clients are within walking distance" (respondent #29)
>
> "General knowledge about what's going on, opportunities to meet people, and [participate] in information sharing" (respondent #46)

Local networking appears to be an effective marketing tool for those providing financial services to the offshore sector itself, and for those serving the domestic market. The next section analyses international marketing efforts involving public and private interaction and networking.

Direct Marketing Efforts

In the mid-1990s the Manx government began to address concerns by the private sector regarding the lack of a unified marketing approach for IOMplc. A report by a London-based public relations consultancy firm reportedly has recommended that the island's government should take a more direct marketing role in the promotion of the offshore financial sector. The Manx Government (1996) recognized that

> competition between offshore centers was becoming increasingly keen and . . . the Isle of Man still suffered from a lack of profile and a poor image in international markets, particularly amongst financial professionals. Additionally it was recognized that the Isle of Man's marketing effort was under-resourced in comparison with its major competitors and this would need to be addressed if the island was not to lose ground as a financial center in the longer term (p. 7).

The view that the Isle of Man suffers from a poor image was reiterated by several survey respondents who mentioned the island's traditional tourist image as one for the "bucket and spade brigade" referring to the working class source of tourists from major urban centers in Northern England, Ireland, and Scotland in the post war years through to the 1970s.

The Commercial Development Division (CDD) of the Manx Treasury was subsequently created in the early 1990s and charged with promoting the island. Promotional strategies take several forms including, first, media campaigns initiated by the CDD targeting key international publications. According to the CDD office, in 1995, the island's offshore sector had appeared as a special survey feature or supplement in 35 different publications.

Second, the *IOMplc Roadshow*--a joint public-private initiative--has already been taken to Switzerland, Hong Kong, and the U.K. The island's use of public-private interaction through the consultative committee process (see Chapter 5) has been applied to recent marketing efforts. Moreover, the consultative process itself is used as a marketing tool being cited as the first of its kind for all OFCs. The *IOMplc Roadshow* consists of a delegation of both government officials and private sector representatives working together to promote the island. Public sector representatives argue that the public-private *Roadshow* approach is optimal as the private sector representatives can address, at first hand, the services they

provide, and the participation of politicians as well as civil servants will open doors and create contacts that may otherwise be closed to the individual firms.

Govemment and private sector participation in exhibitions for particular segments of the offshore sector forms the third strategy. In addition, three marketing executives travel to regions throughout the world to promote the island to financial professionals and increase awareness of the offshore financial services and products available for prospective clients. Target areas for marketing are identified by the Treasury Division and, at the time of the survey, were US, South Africa, and Hong Kong. The CDD also assists in the promotional efforts of other Govemment Departments, in particular for the shipping industry within the Transport Department, and with general conference and corporate initiatives.

The creation of the CDD was seen by many private sector survey respondents as a long-awaited positive move by the public sector. Frustration was exhibited by some respondents at the lack of govemment-led promotion and marketing efforts until recently, resulting in private-sector involvement in the promotion of IOMplc through their own corporate marketing efforts.

Some private sector survey respondents had distinct views on the marketing role of the major *regulatory* bodies (in particular the FSC and Insurance Authority). Some complained that the FSC seemed to take no interest in marketing and promotion and lauded the Insurance Authority for their proactive pro-marketing attitude. Debate over whether regulatory bodies should have a marketing and promotional role is a sensitive one--should regulatory and supervisory bodies exist to do just that, or should they participate in the govemmental efforts to promote the entire financial sector? The existence of this debate was evident from both private and public sector interviews.

Regardless of the perceived role of regulatory bodies in the marketing and promotional process, the literature produced by each of these bodies indicates at least a certain marketing awareness. For example, the most recent annual report of the Financial Supervision Commission (FSC, 1997) states

> The primary aim of the [FSC] is to engender an environment in which financial institutions provide quality products and services for the economic benefit of the island. . . . sometimes referred to as a 'compliance culture'. . . . this reinforces the need for the [FSC] and the market to work closely together, to understand each other better, and to *recognise the roles that each has to play in ensuring the island has a secure and prosperous future.* For it is becoming increasingly clear that jurisdictions like the Isle of Man will be judged on substance rather than form--on the reality of regulation and the reality of financial activity rather than the repetition of pious platitudes abut high standards and quality institutions (p. 3, emphasis added).

The Insurance Authority--perceived as being proactive and market oriented by many survey respondents--produced literature which states

> 'Firm regulation--yes. Red tape--no'. The Insurance Act 1986 is designed to ensure that those who run insurance businesses are fit and proper and that the companies have sufficient resources at all times. This legislation is simple yet thorough and its reporting requirements, while satisfying the Authority's supervisory needs, *do not place unnecessary demands on the marketplace* (1996, p. 4, emphasis added).

The shipping industry's regulatory body (The Marine Administration, 1996), in conjunction with the CDD, promotes the shipping sector by asserting

> The Isle of Man is a leading Northern European Centre for International Shipping Business being close and within easy reach of London and other European centres. In addition, as an international financial centre, it can offer those highly specialised services in banking and finance, insurance, taxation and law that are associated with a reputable offshore jurisdiction. . . . The Government is . . . very conscious of the shipping community requirements, having a *policy to promote the necessary legislation* to offer a diversity of services at competitive costs, to assist ship owners in effectively operating their ships. Beneficial legislation designed to meet their specific needs . . . provide a supportive environment for the shipping community (p. 1, emphasis added).

Manx regulatory bodies therefore do have a marketing stance when producing literature; however, inspection of these documents highlights the differences in internal perceptions of their role as marketers. The FSC appears to have more of a covert marketing role, stressing the creation of the appropriate regulatory regime and the monitoring of that regime as being their major remit. The Insurance Authority and the Marine Administration are more cognizant of their roles as marketers of their respective sectors and play an active role in promotion and marketing activities.

Evidence from the private-sector survey respondents illustrated confusion about the role of the regulatory bodies; however, when analyzed in terms of the *functional activities* each regulatory body is responsible for (i.e., banking, versus insurance, versus shipping) various regulatory stances should be evident. Existing literature almost uniformly acknowledges that any attempts to regulate and supervise the banking industry *must* consider the issues of lender-of-last resort, safety-and-soundness, and the possibility of systematic bank failure which should result in a concomitant prudent and conservative stance (Greenbaum and Thakor, 1995; Lewis and Davis, 1987). Other fields within the offshore sector do not have this structural responsibility and therefore do not have to show the same restraint.

The Isle of Man Chamber of Commerce, with its close relationship to a public-private organization *The Manx Business Connection* (MBC), is another example of an integrated approach to marketing and promotion in the island. MBC was formed in 1993 through sponsorship of the Government Department of Industry and its function is as a marketing tool. The Department of Industry remains involved in the organization, but administration

of MBC is performed by a private sector company which is paid a fee by the government. MBC uses a sophisticated audio-visual marketing presentation, combined with Chamber of Commerce officials and members of the private sector active in the Chamber, to promote the island. Although the Chamber is a self-reliant and independent organization funded solely through private sector participation, its philosophy and concomitant close relationship with the public sector through the MBC and participation in the government consultative committee process illustrates its commitment to the IOMplc concept.

Representatives of both public and private sectors have acknowledged that their joint marketing efforts to promote and increase awareness of the island are necessary to ensure the continued growth of the offshore sector. Chapter 7 concludes this study by considering the merits of this study process, the implications of the findings, and the way ahead both for the island as an OFC and for the study of these small places.

CHAPTER 7
CONCLUSIONS AND THE WAY AHEAD

Growth of the Financial Sector

The Manx financial sector has grown considerably over the past twenty years: most of the growth actually occurred in the last ten years. The financial sector constitutes over 35 percent of the island's GDP; in 1986 the deposit base for Manx licensed banks is over £14 billion, up from £2.5 billion in 1986; the number of collective investment schemes managed in the island is now well over 100, with assets of over £1 billion; the assets managed by insurance companies stand at over £4 billion (*Offshore Outlook*, 1996).

This research has shown that the growth of the Isle of Man's offshore financial services sector has been diversified and multi-faceted by function, comprising the banking, insurance, fund management, investment business, accounting, legal, and shipmanagement industries. The Manx financial sector also is diverse in terms of firm size, ranging from very small firms (1 person operations) to very large firms (over 300 employees). Furthermore, a great deal of diversity is found in the number of source areas of clients and the type of niche financial services provided. Survey findings show that the sector is truly global in terms of its linkages throughout the world with clients, other offices within the corporate network, and financial markets. Niche market areas such as South Africa and Hong Kong were developed through historical or corporate links, and in some cases, personal linkages of individuals now working and residing in the island.

Both corporate and individual participation in networks is an important feature of the island's role as an OFC. A variety of networking activities takes place and the function and role of the networks themselves are multi-faceted. Networks are used by individuals and firms to gain or share information; to help craft the financial services regulatory and supervisory regime; and to act as both an overt and a covert marketing tool.

The Manx financial sector sees other British Isles' OFCs (particularly the Channel Islands) as its major competitors, although this perception is tempered by recent corporate organizational changes, particularly within the banking sector, which has resulted in all of these places working together as the "offshore" arm of their organization. Each OFC is then responsible for different functional activities within the group according to that place's particular competitive advantage. The Isle of Man, because of its relatively low costs of operation and space to grow, appears to be evolving into the more labor-intensive *back-office center* of the British Isles' OFCs.

Sixty private sector survey respondents indicated that Manx financial sector grew in size and importance because of both internal factors (such as the specific regulatory regime put in place by the government in consultation with the private sector, the relative location of the island in between the United Kingdom and Ireland, relatively low costs of operation--particularly when compared to the Channel Islands-- and room to grow) and external factors, in particular the perception that the Channel Islands are "full up".

Revisiting the Role of Regulation

Findings from the survey of 60 firms engaged in providing financial services in the island showed that almost 60 percent stated that the Manx legislative and regulatory framework was very important in driving the growth of business. According to some of the respondents, the importance of regulation was largely connected to the re-establishment of a credible reputation for the island after the collapse of a large savings bank in the early 1980s. With respect to the actual *process* of regulation and supervision, a variety of opinions were proffered from the private sector and, interestingly, they varied according to the specific institution of regulation and supervision involved. Some of those engaged in the provision of banking and investment services suggested that the regulation and supervision had evolved to be too onerous and constricting. Many of those engaged in providing insurance services regarded their regulatory body as being more flexible and real-market driven.

Consensus was shown, though, with respect to the *reputational* role of the legislative and regulatory framework--one of the most critical factors in the minds of members of the private sector is the importance of the island being perceived as a safe, stable and well-regulated OFC. Many respondents suggested that it is a very difficult task to achieve this reputation. "There is a fine line between not enough and too much regulation - it is a balancing act" was a phrase heard several times during the interview process. Not enough regulation means a sub-optimal reputation as an OFC and caution on the part of potential investors--"Cayman, and Turks and Caicos have loose regulation", or "Gibraltar has political instability, lack of space, and bad regulation" (survey respondents). Too much regulation

means that, for firms already established, it is difficult to do business and, more importantly, make profit. "We wanted to introduce a financial product here and in [another OFC]. It took the [Manx] regulators six weeks to give the OK: in the other OFC it was immediate" (survey respondent). This finding supports the work of Hancher and Moran (1989) and, indirectly, Flannery's (1994) argument about government versus marketplace philosophy of regulation.

Moreover--and possibly more importantly from an "offshore" perspective--empirical evidence from the Manx finance sector supports the claim by many that effective regulation and supervision are the key to establishing and maintaining a reputation as a safe, confidential and stable place to invest money.

Networks Revisited

In the Isle of Man, networks play an important role in both the day-to-day business of offshore finance, and the long-term strategic planning and policy efforts to create a superior reputation amongst offshore financial centers. All respondents surveyed in the island belonged to at least one type of business network, and many belonged to several. In fact, one of the few complaints regarding financial services networks (or committees) in the island was that there are too many of them. Some respondents, especially those whose organizations are newcomers to the island, seemed a little overwhelmed by the number of committees and networking organizations, and saw no logic or overall structure to the networking system.

Three types of financial services "actor networks" were identified and linkages to the fourth network--the client network--were analyzed. The system of offshore financial services

networks was shown to be dynamic, both in terms of the networks themselves and the individuals comprising each network. Financial services providers belonged to different kinds of networks (corporate, professional, and/or social) and had several reasons for participating in those networks.

Many respondents belonging to branches or subsidiaries of large transnational organizations used local professional and public-private "policy-driving" committees or networks as a means of participating in the development of the island's regulatory regime which can be seen as a way of indirectly expanding their client-base. Respondents from smaller firms, not part of a large corporate network, used local networks for several reasons, including information sharing and direct marketing strategies.

The sheer number of networking activities is seen by survey respondents as both a positive and a negative feature of the island's offshore sector. The approachability of colleagues and government officials made possible through the thick layering of networks is seen by some as a definite advantage of the island when compared to other places, because this interaction can help speed up legislative changes to the regulatory regime to make it more sophisticated and place the island at the cutting edge of legitimate offshore financial service provision. On the other hand, too many networks and committees are seen by some--particularly those more recent arrivals to the island--as being confusing, inefficient and ineffective. The *number and remit* of local committees operating in the financial services sector were identified as a problems as evidenced by the following statements:

"Who is in charge of all these committees? No-one is and that's a problem" (respondent #25).

"Lower level meetings are more productive. There are lots of meetings, but how much action?" (respondent #8).

"The [functional] network tries to be the umbrella, but our [sector] has three diverse areas and our needs are not addressed" (respondent #60).

"[Professional associations are] skewed toward the 'big' players, but good for the smaller players to input as a group" (respondent #23).

Public-Private Interaction as an Economic Development Strategy

The deliberate establishment of a specific regulatory environment through the use of continuous public-private interaction was (and still is) used as a tool for successful economic development. This strategy of economic development has been identified recently by Leicht and Jenkins (1994), and Hastings (1996) has suggested that the *policy synergy* which can occur through this type of interaction is invaluable. Using a thorough process of continuous public-private interaction through the Consultative Committee framework, the island's function as a reputable OFC has been established and solidified over the past decade. So, as a process of "bottom-up" economic development, public-private dialogue to craft the island's financial legislative framework appears to have been successful. In the Isle of Man, a mix of proactive and reactive regulatory standards and supervisory practices have been established by the government and the private sector through a process of deliberate and continuous interaction.

Overt strategies to market *IOMplc*--particularly the use of the *IOM Roadshow*, and the Manx Business Connection--also involve heavy public-private interaction and

cooperation. The notion that "we are all in this together" seems to have become more widely accepted since the government, through the Treasury Department's Commercial Development Division (CDD), has shown a greater interest and commitment to promoting the island and its offshore financial sector.

Most of the 71 public and private respondents in this survey agreed that the *image* of the Isle of Man as a *reputable* offshore center has improved tremendously since the crash of a major savings bank there in the early 1980s. What appears to be missing still, though, is the awareness and acceptance of the Isle of Man as a *sophisticated, global offshore financial center* by financial professionals throughout the world. The Isle of Man has international linkages particularly to such places as the Middle East, Hong Kong, and South Africa, but in much of the rest of the world near-total lack of awareness appears to exit on the part of financial professionals--those who are in the business of managing other peoples' and institutions' money. It is linkages with these people that appear to be the way forward.

The Future

This study has raised a number of possibilities for future study and the rest of this chapter considers future research in the light of the findings presented so far. Future directions will be considered in three different ways: first, implications of structural changes in the offshore financial industry will be addressed; second, recommendations for future marketing and development strategies for the Isle of Man will be developed based upon survey findings; and third, future directions for the study of other OFCs based on the research process used for this case study will be presented.

Implications of Structural Changes in the Offshore Financial Industry

One of the themes identified by some survey respondents in the Isle of Man, and reported with increasing frequency in the financial literature, is the changing nature of financial services provision with the increasing trend toward "one-stop shopping" for financial services and products. Consumers of financial services are demanding convenience and efficiency from financial institutions, and the financial services industry has responded by striving to increase the number and variety of financial products and services they offer. This trend has, of course, a regulatory dimension in that the political infrastructure of a country has to allow this functional diversification to take place. The United States has struggled, for example, with the separation of commercial and investment banking functions established by the Glass-Steagall Act.

For OFCs, this provides an opportunity for *regulatory arbitrage* as reactive, reflexive, and proactive legislative changes can occur *quickly* because of the (usual) smallness of the place and the familiarity of most financial practitioners, government officials, and politicians. This surely is an opportunity for those engaged in offshore services provision to develop legitimate innovative services and products to satisfy the demands of those wishing to have at least some of their wealth managed offshore.

This trend also has implications for the offshore firms themselves as they aim to provide more services in-house. Many of the most highly skilled offshore practitioners have professional qualifications in more than one field (for example, in accountancy and law) or banking and law, and are sought by both private sector firms and regulatory institutions.

Furthermore, many firms have developed cross-functional professional alliances to ensure that if the clients' demands cannot be fully serviced in-house, they can be met though the close professional relationship between that firm and another providing the extra service or product needed.

Additional offshore reaction to this trend is evident with the recent spate of multi-national corporate reorganization into "offshore" groupings, particularly within the banking industry. Most 'high-street' banks have now instigated their own intra-corporate "offshore" groups placing all the British Isles' OFCs (and, in some cases, other more geographically dispersed OFCs) underneath the same organizational umbrella. This appears to be an attempt to create distinct spatial divisions of labor to take advantage of each OFC's comparative advantages to provide the best one-stop service for the client.

What are the future implications of this trend of one-stop shopping for OFCs? Increased diversification of services and products within firms known for their 'traditional' services of banking, insurance or accountancy is likely as firms attempt to develop total wealth management strategies for their clients. This appears to be somewhat in contrast to the onshore world, where reaction to the changing nature of financial service provision is being played out with a great deal of publicity within the accountancy field: the 'Big Six' will probably become the 'Big Four' through mergers and acquisitions; and one firm is 'divorcing' its consulting arm from the rest of its traditional accountancy and audit functions.

Future Directions for the Isle of Man

The Manx offshore financial sector has shown considerable amount of functional and geographic expansion over the past ten years. What needs to be done to ensure that continued growth takes place and that future growth can be well-managed? Based upon the findings from this study a number of strategies are suggested. First, the Isle of Man should continue with its strategy of using public-private interaction in efforts to promote IOMplc. Constant scanning activities should take place to monitor the structural changes in the financial industry as a whole, and subsequently identify ways in which new and innovative offshore services and products can be researched and developed to put the island at the cutting edge of offshore financial service provision. Close monitoring of macroeconomic conditions and changes within targeted market areas (for example, the United States and Argentina) should be undertaken by both public and private sectors, and regular dialogue between the two sectors instigated in the form of a *structural strategic planning steering committee*. Furthermore, this institution could be used to identify new target markets and populations. General wide-ranging discourse between those in the public and private sectors interested in furthering the general goals of IOMplc would place the island in a proactive position for future sophisticated and leading edge developments as a complete wealth management center.

The concern by some of "disorder" in the number of committees and networks, and confusion over the responsibilities and tangible evidence of utility of networking activities, could be addressed by the adoption of a *gatekeeper* to whom all external enquiries and all

outreach activities would focus. This strategy of economic development is increasingly being adopted within local manufacturing centers in Europe and the United States (Malecki, 1997a). This person's remit would be to function in a public relations role[1], having intimate knowledge of both inwardly focused networking and strategic alliances, and outwardly focused marketing and promotional efforts.

Concern regarding the outward appearance of the island, particularly portions of the capital, Douglas, where most of the offshore activity takes place, was expressed by several survey respondents. The words "tatty" and "run-down" were used by more than one respondent expressing concern about the lack of polish and sophistication of the outward appearance of the island[2]. The island's central and local governments surely have a joint responsibility to support the financial services sector in its quest for sophistication and polish. This needs to happen not just in the intangible world of regulation and supervision, but in the tangible arena of urban landscape and infrastructure. In some sectors of the offshore financial world, clients do not have anonymous electronic identities, but are real people needing or wishing to visit the island in person. The perception of quality has to be omnipresent.

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[1]Some survey respondents acknowledged that a similar strategy is already in place in Jersey and identified the individual functioning in that role.

[2]This concern was especially apparent when respondents were comparing the island with the Channel Islands, which have the outward appearance and visible perception of "quality". The Isle of Man's new and rapidly growing film industry utilizing, amongst other things, the scenic natural landscape to attract film-makers is seen by many as a move away from the perception of the island as an aging and tatty destination for the "bucket and spade tourist brigade" mentioned previously and a step in the right direction to promote the island as a quality jurisdiction.

Further Study of OFCs

Intimate knowledge of the Isle of Man and first-hand exposure to the changes taking place in the island's economy during the 1970s and 1980s were a luxury afforded to me as a native. This cannot be repeated, but insight gained into the study *process* provided some valuable insights to avenues for further research. All respondents interviewed for this study were happy to give their time, but were most comfortable giving information their way rather than sticking to a rigid questionnaire format. Future research should more finely craft open-end questions and possibly consider the use of a tape-recorder to accurately capture interviews[3].

Important findings identified from this study include: quantity versus quality labor issues and work-permit problems; public-private interaction in both the regulatory process and the marketing process; specific global linkages; and perception of competition and how to "lead the pack" rather than follow. Future research could construct a similar survey process with one or more of the island's competitors to construct a comparative study to identify similar (or dissimilar) strategies for success. To use Amin and Thrift's (1993) nomenclature "institutional thickness" in the Isle of Man is the driving force behind its success over the past decade--is this the same in other OFCs?

Finally, one altruistic comment by a representative from a large firm providing both offshore and domestic services in the Isle of Man captures the spirit of this local solidarity

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[3]This technique has, of course, been used extensively in anthropological research (Coffey and Atkinson, 1996). I did not even consider asking to tape interview because of the sensitive nature of the subject, but this might be a useful way to capture the complete richness of the data.

and indeed of the respondents themselves, who so generously gave their time during the interview process:

"We get a lot out of the island so we put a lot back".

APPENDIX A
ISLE OF MAN FINANCIAL SERVICES SECTOR QUESTIONNAIRE

SECTION ONE: GENERAL INFORMATION

1.1 What type of SERVICES are provided by your company?
1._____
2._____
3._____
4._____

1.2 Do you consider that any of the services named above serve a particular NICHE MARKET? (In other words, is your company providing something UNIQUE or different?
If YES, can you elaborate?
_____
_____

1.3 How many people are currently EMPLOYED in your company in the I.O.M?_____

1.4 What is the OWNERSHIP STRUCTURE of your company (partnership, single firm, branch office, subsidiary, etc.)? _____

If BRANCH, where is your HQ? _____

If BRANCH, where are the other branches that you contact most frequently located?
_____
_____

For BRANCH FIRMS only, what advantages does location in the Isle of Man offer your firm that cannot be found in branches elsewhere?
_____
_____

1.5 How LONG has your company been in the ISLAND? _____

1.6 How many employees did your company have when you were FIRST ESTABLISHED in the island?

_____

[1.7 If 1.3 is greater than 1.6, what are the MAJOR REASONS for growth?

_____

_____

_____

SECTION TWO: LINKAGES

I. External to I.O.M.

2.1 Which PLACES in the world does your office communicate with on a daily basis?
CITIES:_____
COUNTRIES:_____
OTHER OFCs: _____

2.2 What MEANS OF COMMUNICATION is most commonly used?
_____ (a) Telephone
_____ (b) Fax
_____ © Computer network (WAN)
_____ (d) Computer network (WWW/Internet)
_____ (e) Other (specify)_____

II. Internal to I.O.M

2.3 On the island, what kind of people do you communicate with on a daily basis?
_____ (a) Clients
_____ (b) other financial firms offering similar services
_____ © other financial firms offering complementary services (specify)
_____ (d) Manx institutions (government departments, FSC, etc.)
_____ (e) other (specify)_____

2.4 What MEANS OF COMMUNICATION is most commonly used?
_____ (a) Telephone
_____ (b) Fax
_____ © Computer network (WAN)
_____ (d) Computer network (WWW/Internet)
_____ (f) Other (specify) _____

III. NETWORKS

2.5 Does your company belong to any FORMAL NETWORKING organizations? (Chamber of Commerce, business groups etc.)
If YES, are they:
LOCAL (I.O.M.) name: _____
NATIONAL name: _____
INTERNATIONAL name: _____

2.6 What is the PURPOSE of membership in the organizations named above?
LOCAL_____
NATIONAL _____
INTERNATIONAL _____

2.7 Does your company participate in any INFORMAL NETWORKING groups?
If YES, name and purpose:
_____
_____
_____

SECTION THREE: PERCEPTIONS

I would now like to ask you about YOUR VIEWS on the I.O.M. as an OFC by asking you to think about the IMPORTANCE of the following issues. For each issue I would like you to tell me if that issue is VERY important; SOMEWHAT important; of LITTLE importance; of NO importance whatsoever.

Legislation

3.1 How important are changes in government legislation in the growth of the financial services sector over the past 20 years? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

Which specific ACTS OF TYNWALD have influenced YOUR COMPANY'S:
INITIAL PRESENCE on the island:_____
SUCCESS over the past 20 years: _____

3.2 How important are the island's comparatively LOW TAX RATES in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

3.3 How important are the island's comparatively LOW COSTS in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

Supervision

3.4 How important was the ESTABLISHMENT of the FSC in explaining the growth of the MANX FINANCIAL SERVICES SECTOR? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

3.5 How important is the FSC's CURRENT AGENDA in explaining the recent growth of the MANX FINANCIAL SERVICES SECTOR? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

3.6 Are there any OTHER INSTITUTIONS (govemment departments, public/private organizations, etc.) that have played a crucial role in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?
If yes, name and importance:

_____

3.7 Are there any KEY INDIVIDUALS who have played a crucial role in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?
If yes, name and importance:

_____

Technology

3.8 How important are the island's existing TELECOMMUNICATIONS TECHNOLOGY in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

3.9 Are there any telecommunications TECHNOLOGIES that you would like to see ADDED to the island's infrastructure?
If **YES**, please specify

_____

_____

Other factors

3.10 How important are the following Manx characteristics in explaining the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years? (circle):
(a) political relationship with the U.K.:
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE
Specify_____
_____

(b) location: **EXTREMELY, QUITE, MODERATELY, LITTLE, NONE**

Specify_____
_____

© QUALITY of the labor force:
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE

Specify_____
_____

(d) QUANTITY of the labor force:

EXTREMELY, QUITE, MODERATELY, LITTLE, NONE
Specify_____
_____

3.11 How important are BUSINESS NETWORKS (Section TWO.III) in explaining the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years? (circle):
EXTREMELY, QUITE, MODERATELY, LITTLE, NONE
Specify_____
_____

3.12 Where is your primary client base located?

3.13 Where do you see your greatest competition at present? (jurisdiction and/or firms)

3.14 How do you generate new business?

3.15 Other comments:

APPENDIX B
SUMMARY REPORT OF FINDINGS

The following report was sent to all the survey respondents in January, 1997.

GLOBAL FINANCE AND OFFSHORE FINANCIAL CENTERS:

A CASE STUDY OF THE ISLE OF MAN[1]

SUMMARY REPORT OF FINDINGS - JANUARY 1997

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I. INTRODUCTION

Amongst those involved in any aspect of the financial sector, consensus exists regarding two important trends: the rapid growth of the sector itself over the past twenty years, and the amount of complexity that has accompanied this growth. The aim of this study was to interview actual practitioners of offshore finance in order to obtain their perspectives and understandings of the reasons behind the growth of the sector in the Isle of Man. This summary report of findings is drawn from a survey of 60 firms engaged in providing financial services in the island.

II. METHODOLOGY

Via a series of personal interviews with those actively involved in the provision of financial services in the Isle of Man, perspectives were gathered regarding the growth of the island as an international offshore financial centre (OFC). A sample of 20 percent of all firms engaged in providing financial services was drawn from information published by the Isle of Man Government Finance Factfile (1995), and the Financial Supervision Commission's Annual Report (1995), which together listed all practitioners in the sector. The resulting sample size was 68 private sector firms, ranging from banks and building societies, to life and captive insurance companies, to accountants, lawyers, ship management companies, and others. The final completed sample size was 60, due to the refusal of some firms to participate in the study, and the doubling-up of listings from government sources. The private sector sample was complemented by a survey of 15

representatives within the public sector, in order to capture the difference in perspectives (if any) from the different sides of the financial services sector. One difference which became apparent during the survey itself, was the perceived role played by each side in marketing and promoting the island as an OFC. Many of the private sector respondents felt that they alone were responsible for promoting the island until very recently, whereas the public sector respondents had a much more positive outlook on their marketing role.

III. PRELIMINARY DATA ANALYSIS

Table 1 shows the *type* of service provided by the sample firms. The total number of services (82) is greater than the total number of firms (60) because some firms offer more than one type of service. In particular, some of the larger institutions offer most of the services shown in the table. The situation is further complicated by the fact that different types of firms offer the *same* type of financial services, e.g., company/trust formation services are provided by accountancy firms, banks, investment companies, and advocates (lawyers).

[Table 4.3.]

The difference between producer services and consumer services is exemplified by the functional roles of accounting firms. Some provide "domestic" (producer) services which either (a) service the financial sector (e.g., audit services for banks), or (b) service the rest of the Manx economy (e.g., audit services for manufacturing firms, retailers, farmers, etc.). Others provide domestic services *and* direct offshore financial services to expatriate clients and high net worth individuals (HNWI) living in the island and are competing directly with other offshore financial institutions in the Manx sector.

Identification of a specific niche market or niche product is shown in table 2. Sixteen firms identified their niche as provision of specific services for a specific type of client such as tax planning, insurance, and shipmanagement. The provision of specific financial products or instruments was the second largest "functional" niche identified by survey respondents. The most common "geographic" niche is service provision for UK expatriate clients, followed by international offshore clients (defined as non-residents of the Isle of Man located throughout the globe).

The recent vibrancy of the island's finance sector is illustrated by figure 1 which shows the number of years firms have been doing business in the island. Over half of the firms are less than 11 years old and more than three-quarters are less than 25 years old. A handful of firms have been present on the island for over 100 years; they obviously served the domestic market until recently, but now some of them have adapted to provide offshore services in addition to domestic services although some have not. A fairly even distribution in firm size is found, ranging from one-employee operations to firms

employing over 300 people. Some of the smaller firms are new but some or all of their *personnel* have been on the island working in the financial sector for longer, but with a different firm, usually in the accountancy field. All types of firms surveyed have experienced growth in the past ten years leading to the conclusion that the growth of the financial sector is multi-faceted and not reliant solely on one particular type of service such as "banking", "insurance" or "shipmanagement".

[Table 6.1]

[Figure 4.2]

Indication of how the Isle of Man links into the rest of the world is illustrated in table 3. Survey respondents were asked which parts of the world their offices were in contact with on a daily or very regular basis. Distinct patterns emerged with an evident *proximity* effect illustrated by the large number of linkages with the U.K., Ireland, and other E.U. countries. Large numbers of linkages also take place with North America, other offshore financial centers throughout the world, South Africa, and the Middle East. These linkages comprise every type of business communication - be it with clients, financial markets, or other offices within the specific corporate network. Many of the linkages to other OFCs are with other offices in the corporate organization illustrating the trend of establishment of "offshore" groups within the corporate organization. This trend is particularly evident within the banking sector.

[Table 4.6]

Survey respondents were asked who they considered their major jurisdictional competition to be. Table 4 shows that the Channel Isles are perceived to be the major competition for the Isle of Man, followed by Dublin (IFSC). Furthermore it was evident that OFC competition varies by function -Jersey for banking; Guernsey for captive insurance; Dublin, Luxembourg for fund management.

[Table 6.2]

Survey respondents' perceptions regarding the reasons for the growth of the financial sector in the Isle of Man are shown in table 5. Almost half of the survey respondents identified the establishment of a specific regulatory environment in the island as a major reason for the growth of the sector. Almost one-third of the respondents identified "location" as an important factor -this can be interpreted both as physical proximity to service the British Isles' market, and as a time zone factor (Europe rather than in the Caribbean or Asia). Specific attributes of the Isle of Man such as lower costs of operation and room to grow were mentioned by almost one-third of the survey respondents. This ties into the next most popular reason - the acknowledgment that the Channel Islands are "full-up" leading to an assertion by many survey respondents that the

growth of the Manx financial sector "has been growth by default".

[Table 5.1]

However, this somewhat negative conclusion drawn by some of the survey respondents is tempered by the recent initiatives put in place by the Manx Government and by the private sector (for example, the Manx Business Connection) to actively *promote* and *market* the island as a safe, confidential and reputable *wealth management centre*.

IV. CONCLUSIONS

There is no doubt that the Manx financial sector has grown considerably over the past twenty years: moreover, most of the growth occurred over the last ten years. The financial sector constitutes over 35 percent of the island's GDP; the deposit base for Manx licensed banks is over £14 billion, up from £2.5 billion 10 years ago; the number of collective investment schemes managed in the island is now well over 100, with assets of over £1 billion; the assets managed by insurance companies stands at over £4 billion.[2]

The preliminary findings reported here indicate that:

* the island's financial sector has **grown** considerably over the past ten years

* this growth is **diversified and multi-faceted** comprising the banking, insurance, investment business, accounting, and shipmanagement industries

* the Manx financial sector also is **diverse** in terms of firm size and financial services provided

* the sector is truly **global** in terms of its linkages throughout the world with clients, other offices within the corporate network, and financial markets

* the Manx financial sector sees other British Isles' OFCs as its major **competition**

* the Manx financial sector grew in size and importance because of both **internal factors** (regulation, location, low cost, room to grow) and **external factors** (the Channel Isles are "full up")

One area of concern reported by several survey respondents was the lack of a cohesive marketing strategy for "Isle of Man plc". In the past couple of years this concern has begun to be addressed by the government and - more importantly, from an economic development perspective -*public/private interaction*. This is best exemplified by the

Treasury's *consultative committee* process; the expanded role of the *Commercial Development Division* of the Treasury; and the development of the Isle of Man plc *"roadshow"*.

V. ENDNOTES

1. Research funded by NSF Grant #SBR-9600490

2. *Offshore Outlook*, 1996, **3**, p. 2.

APPENDIX C
ISLE OF MAN FINANCIAL SERVICES SECTOR QUESTIONNAIRE
SELECTED AGGREGATE SUMMARIES

SECTION ONE: GENERAL INFORMATION

1.1 What type of SERVICES are provided by your company?

see Table 4.3

1.2 Do you consider that any of the services named above serve a particular NICHE MARKET? (In other words, is your company providing something UNIQUE or different?

If YES, can you elaborate?

See Table 6.1

1.3 How many people are currently EMPLOYED in your company in the I.O.M?

See Table 4.5

1.4 What is the OWNERSHIP STRUCTURE of your company (partnership, single firm, branch office, subsidiary, etc.)?

Subsidiary - **70%**
Independent - **30%**
(N = 60)

Where is your HQ?

Isle of Man - **30%**
British Isles - **34%**
Other - **36%**
(N = 60)

If BRANCH, where are the other branches that you contact most frequently located?

British Isles - **44%**
Other - **56%**
(N = 39)

For BRANCH FIRMS only, what advantages does location in the Isle of Man offer your firm that cannot be found in branches elsewhere?

See Table 5.1

1.5 How LONG has your company been in the ISLAND?
See Table 4.4

1.6 How many employees did your company have when you were FIRST ESTABLISHED in the island?
Mean = **6.2 employees**
(N = 48)

[1.7 If 1.3 is greater than 1.6, what are the MAJOR REASONS for growth?
See Table 5.1

SECTION TWO: LINKAGES

I. External to I.O.M.

2.1 Which PLACES in the world does your office communicate with on a daily basis?
See Table 4.6

2.2 What MEANS OF COMMUNICATION is most commonly used?
Telephone - **100%**
Fax - **94%**
Computer: e-mail - **29%**
Computer: WAN - **12%**
Mail - **21%**
(N = 51)

II. Internal to I.O.M

2.3 On the island, what kind of people do you communicate with on a daily basis?
See Table 4.7

2.4 What MEANS OF COMMUNICATION is most commonly used?
Telephone - **100%**
Fax - **83%**
Face to face - **86%**
Mail - **52%**
(N = 58)

III. NETWORKS

2.5 Does your company belong to any FORMAL NETWORKING organizations?
See Table 4.8

SECTION THREE: PERCEPTIONS

I would now like to ask you about YOUR VIEWS on the I.O.M. as an OFC by asking you to think about the IMPORTANCE of the following issues. For each issue I would like you to tell me if that issue is VERY important; SOMEWHAT important; of LITTLE importance; of NO importance whatsoever.

Legislation

3.1 How important are changes in government legislation in the growth of the financial services sector over the past 20 years?
See Tables 5.3, 5.4

3.2 How important are the island's comparatively LOW TAX RATES in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?
See Table 5.2

3.3 How important are the island's comparatively LOW COSTS in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?
See Table 5.1

Supervision

3.4 How important was the ESTABLISHMENT of the FSC in explaining the growth of the MANX FINANCIAL SERVICES SECTOR?

Extremely - **39%**
Quite - **39%**
Moderately - **12%**
Little - **10%**
None - **0%**
(N = 51)

3.6 Are there any OTHER INSTITUTIONS that have played a crucial role in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?

Commercial Development Division
Department of Industry
Tax Assessor's Office
Treasury Department

Technology

3.8 How important are the island's existing TELECOMMUNICATIONS TECHNOLOGY in the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?

Extremely - **50%**
Quite - **44%**
Moderately - **10%**
Little - **6%**
None - **0%**
(N = 50)

3.9 Are there any telecommunications TECHNOLOGIES that you would like to see ADDED to the island's infrastructure?

No

Other factors

3.10 How important are the following Manx characteristics in explaining the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years? (circle):
(a) political relationship with the U.K.:

Extremely - **18%**
Quite - **45%**
Moderately - **18%**
Little - **6%**
None - **12%**
(N = 33)

(b) location:

Extremely - **59%**
Quite - **15%**
Moderately - **0%**
Little - **7%**
None - **19%**
(N = 32)

(c) QUALITY of the labor force:

Extremely - **7%**
Quite - **28%**
Moderately - **19%**
Little - **39%**
None - **6%**
(N = 53)

(d) QUANTITY of the labor force:

Extremely - **38%**
Quite - **23%**
Moderately - **30%**
Little - **9%**
None - **0%**
(N = 53)

3.11 How important are BUSINESS NETWORKS in explaining the growth of the MANX FINANCIAL SERVICES SECTOR over the past 20 years?

See Figure 5.9

3.12 Where is your primary client base located?

Global - **57%**
Isle of Man - **30%**
British Isles - **13%**
(N = 60)

3.13 Where do you see your greatest competition at present? (jurisdiction and/or firms)

See Table 6.2

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BIOGRAPHICAL SKETCH

Sharon Corkill Cobb was born and brought up in the Isle of Man, British Isles. After graduating from the University of Sheffield, England, and Manchester Polytechnic, England, she moved to Moscow, Idaho for graduate study. She met her husband in Idaho and, soon after graduating with a Masters degree, they both moved to Virginia where their son, William, was born. After teaching spells at James Madison University, Harrisonburg, Virginia, and Florida Atlantic University, Boca Raton, Florida, and work as a community planner for a non-profit planning agency in Jacksonville, Florida, the Cobb family moved to Gainesville where their second child, Ellie, was born three months into Sharon's Ph.D. program.

Sharon hopes to reconcile her professional goals with her husband's career plans by finding an academic position in a location suitable to both.

I certify that I have read this study and that in my opinion it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Doctor of Philosophy.

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